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Retirement Security Through Asset Protection: The Evolution of Wealth, Privilege, and Policy

John K. Eason*

This Article examines post-1974 progressions in congressional and judicial thinking about asset protection as it relates specifically to the attainment of federal retirement policy goals. The Article first considers the link between historical trust protections and modern federal retirement policy. That analysis reveals a more recent trend towards defining the scope of retirement plan asset protection by reference to statutory rules that grant favorable treatment to certain "retirement" savings devices. Those rules provide an incentive for funding future retirement through current savings. This Article explains how, and why, asset protection could be similarly tailored to foster retirement income security goals. Inconsistencies in the protections currently afforded, however, call into question the logic of the existing retirement plan asset protection framework. This Article ultimately argues that Congress should incorporate a more comprehensive view of asset protection into federal retirement policy. After explaining the objectives of federal retirement policy and the modern evolution of retirement plan asset protection, the author develops this argument by evaluating the usefulness of retirement policy objectives as a benchmark for establishing asset

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protection boundaries—both within the retirement plan setting and in the context of more traditional trust devices.

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I. Introduction

When the fraudulent activities of corporate executives recently decimated the retirement savings of thousands of employees, a media frenzy erupted and a legislative response ensued.¹ Popular support and pressure for this response originated from the widely held belief that workers should "not lose the retirement benefits that they ha[ve] worked for throughout their lifetimes."² Calls for the partial privatization of the primary public source of retirement income—Social Security—also are appearing more prominently on the agenda

1. This reference is to the Enron Corporation and the thousands of Enron employees who lost over \$1,000,000,000 in retirement savings when corporate scandal led to what was, at the time, the largest bankruptcy in U.S. history. See S. REP. NO. 107-226, at 2–18 (2002) (setting forth the history of the Enron debacle as background to one of the more significant legislative responses, the Protecting America's Pensions Act of 2002, S. 1992, 107th Cong.). See generally U.S. GEN. ACCOUNTING OFFICE, GAO-02-745SP, ANSWERS TO KEY QUESTIONS ABOUT PRIVATE PENSION PLANS iii–iv (2002) [hereinafter GAO-KEY QUESTIONS] ("The financial collapse of the Enron Corporation and other recent corporate failures, and their effects on the companies' workers and retirees, have prompted policymakers and the public to want to know more about private pensions and the benefits these plans provide."), available at <http://www.gao.gov>.

2. S. REP. NO. 107-226, at 3. The broader concept of retirement income security as a component of federal policy is discussed *infra* Part III.

of federal policymakers.³ Such privatization plans most often envision the diversion of Social Security tax revenues into individual worker accounts that produce retirement benefits gauged by investment returns.⁴ Privatization opponents object on grounds that a diversion of funds into such accounts would jeopardize the dependability of Social Security as a source of retirement income, given the unpredictability of private investments not underwritten by the federal government.⁵

Equally important, though perhaps less sensational than the blatant fraud underlying the Enron debacle or the partisan attacks attending Social Security privatization, is another pervasive risk to the security of retirement incomes. The risk is that unanticipated financial circumstances will result in the forced diversion of retirement assets from their intended use to the payment of creditor claims.⁶ That risk is a particular concern when the assets at issue are available to tempt creditors precisely because the individual debtor has diligently taken advantage of federally supported savings devices in order to better provide for her retirement.⁷ Where time (for those currently working) or another source of

3. For an example of legislative proposals taking opposing stances on the issue of Social Security privatization, compare the Individual Social Security Retirement Accounts Act of 1999, H.R. 874, 106th Cong. (supporting the privatization of Social Security) with the Rejecting Social Security Privatization Act of 2002, H.R. 5541, 107th Cong. (opposing the privatization of Social Security). The Social Security program and its relation to private retirement arrangements are discussed *infra* Part III.A.

4. For details on the privatization plans, see the legislative proposals cited *supra* note 3 and see Symposium, *Social Security: Can the Promise Be Kept? A Conference on the Legal, Economic, and Practical Implications of Social Security Reform*, 58 WASH. & LEE L. REV. 1197 (2001). See *infra* notes 70–74 and accompanying text for an explanation of the means by which Social Security is financed.

5. See, e.g., Regina T. Jefferson, *Privatization: Not the Answer for Social Security Reform*, 58 WASH. & LEE L. REV. 1287, 1306–16 (2001) ("As a mandatory social insurance program, Social Security should not be structured to reward the most fortunate [investors]."); Greg Hitt, *Social Security Plan Stalls: Stock Market's Slide Undermines Support for Privatization*, WALL ST. J., July 23, 2002, at A4 (noting reports that individuals would have lost a collective \$31 billion if 2% of Social Security tax revenue had been invested in private accounts since 1998).

6. See, for example, the remarks that Senator Edward Kennedy (D-Mass.) makes in support of greater protection for retirement savings in bankruptcy. 147 CONG. REC. S2151 (daily ed. Mar. 12, 2001). Senator Kennedy explains by example that "retirement money that has been paid in over a lifetime . . . can be eliminated, wiped out, in 4 days of catastrophic illness in a hospital." *Id.* Senator Kennedy further notes in the context of this bankruptcy debate that "[o]ne of the greatest domestic policy challenges facing Congress is the challenge of ensuring that elderly Americans do not live in poverty. After a lifetime of hard work, senior citizens deserve a secure and comfortable retirement." *Id.* at S2149.

7. *Infra* Part III discusses the federally-sanctioned retirement devices referred to and the specific federal incentives granted to those who utilize those devices.

income (for those already retired) to replenish retirement funds is lacking, the concern is magnified and becomes an issue for society in general.⁸

Congress is attuned to this concern and expressly embraces the idea that individuals should have adequate income during their postemployment years.⁹ Federal policies promote this "retirement income security" objective through the implementing mechanisms of Social Security, employer-sponsored pension plans, and private personal savings.¹⁰ Among the myriad of tax, labor, and entitlement legislation enacted in furtherance of this retirement income security goal, Congress included the seemingly straightforward rule that an individual's interest in certain retirement arrangements is inalienable—that is, protected from the claims of the individual's creditors by virtue of a specific limitation upon the individual's right to transfer the interest, either voluntarily or under compulsion from creditors.¹¹ This rule provides a means of "asset protection"¹² comparable in form and substance to the restraint on alienation typically found

8. When creditor claims force a diversion of retirement assets that cannot realistically be restored by the individual, the burden of supporting the retiree would fall entirely upon public programs. See *infra* Part III (discussing public and private funding of retirement).

9. See, e.g., 29 U.S.C. §§ 1001b(a), (c) (2000) (discussing pension plans). The Act states:

The Congress finds that . . . pension plans have a substantial impact on interstate commerce and are affected with a national interest . . . [and that] the continued well-being and retirement income security of millions of workers, retirees, and their dependents are directly affected by such plans It is hereby declared to be [congressional] policy . . . to encourage the maintenance and growth of . . . pension plans . . . [and] to increase the likelihood that participants and beneficiaries . . . will receive their full benefits."

This federal policy is explained more thoroughly *infra* notes 57–64 and accompanying text. The quoted language introduces one of the more complex and pervasive statutory regimes currently in force. See Employee Retirement Income Security Act of 1974 (ERISA), Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C. (labor provisions) and 26 U.S.C. (tax provisions)) (implementing ERISA).

10. See *infra* Part III (explaining in detail these mechanisms, which are commonly referred to as the three legs of the retirement income security stool).

11. See 26 U.S.C. § 401(a)(13) (2000) (defining the assignment and alienation of trusts); 29 U.S.C. § 1056(d)(1) (2000) (same). These sections are more fully discussed *infra* notes 28–33 and 103–28 and accompanying text.

12. The term "asset protection" used here refers to the idea that property or interests in property are to some extent immunized from seizure by, or liquidation on behalf of, an individual's creditors. Among other approaches, asset protection often is achieved through careful selection of the type, location or governing terms of the assets or interest sought to be sheltered. Asset protection planning therefore requires knowledge of many distinct disciplines. See generally *Asset Protection Strategies: Planning with Domestic and Offshore Entities*, 2002 A.B.A. SEC. REAL PROP. PROB. & TR. L. xxiii (Alexander A. Bove Jr. ed.) ("A well thought-out asset protection plan requires expertise in property law, domestic and international tax law, estate planning, the law of trusts and estates, bankruptcy, and debtor-creditor law.").

in state trust doctrine and historically referred to as a spendthrift provision.¹³ This protection is comparable, but not identical, because the last decade of jurisprudence has distinguished the retirement plan restraint on alienation as a protective device entitled to heightened deference.¹⁴ Where protection from creditors fails because such deference is not forthcoming or because a restraint is simply absent as a feature of the retirement plan, other protective mechanisms like bankruptcy exemptions may yet shield the interest from the grasp of creditors.¹⁵ Regardless of the particular avenue to retirement plan asset protection, the legal stakes are high. Federally endorsed private retirement arrangements now hold over \$7 trillion in assets and represent a significant source of financial security for the aging American population.¹⁶ Retirement plan asset protection is therefore becoming an increasingly important aspect of the broader retirement income security goal.

13. See *infra* note 18 regarding the nature and enforceability of anti-alienation restraints in traditional trust doctrine. Traditional spendthrift trust doctrine and the policy debates surrounding asset protection in that context are explained *infra* Part II.

14. See *infra* Part IV regarding the judicial development of a relationship between historical spendthrift trust analysis and the application of restraints on alienation in the context of retirement plans.

15. Bankruptcy exemptions are discussed *infra* Part IV.A.2.

16. See STAFF OF JOINT COMM. ON TAX'N, 107TH CONG., JCX-9-02, PRESENT LAW AND BACKGROUND RELATING TO EMPLOYER-SPONSORED DEFINED CONTRIBUTION PLANS AND OTHER RETIREMENT ARRANGEMENTS 34 (Comm. Print 2002) [hereinafter JCX-9-02] (noting that, as of December 31, 2000, defined benefit plans held \$2.06 trillion, defined contribution plans held \$2.53 trillion, and individual retirement accounts held \$2.65 trillion), *available at* <http://www.house.gov/jct/x-9-02.pdf>. These variations on the types of retirement savings vehicles are described in detail *infra* Part IV. The term "retirement plan" is used in this Article to refer generically to a trust, plan, account or similarly identifiable mechanism that is: (1) voluntary; (2) tax-favored in some manner, such as the availability of pre-tax funding and tax-exempt earnings growth; and (3) purportedly granted preferential tax status in order to encourage its use as a means of savings for retirement. Thus, "retirement plan" as used here does not distinguish in each instance between defined benefit plans, defined contribution plans, individual retirement accounts, or plans for self-employed persons. Where such distinctions are of particular importance, the distinction will be directly stated or clearly implied from the context.

As to the aging of America, demographic trends provide another objective measure of the growing importance of these retirement policy concerns. See SOC. SEC. ADVISORY BD., SOCIAL SECURITY: WHY ACTION SHOULD BE TAKEN SOON 5-7 (rev. ed. 2001) (discussing demographic trends in America over the next seventy-five years), *available at* <http://www.ssab.gov/action/shouldbetaken.pdf>. Those trends show that the number of persons intimately and immediately affected by the security of their retirement income is on the verge of a significant upswing. For example, the first of the "baby boom" generation will retire at age sixty-five in 2011, and by 2030 over 20% of the United States population will be over sixty-five years of age and have an average life expectancy—meaning period for which retirement income must be sufficient—of twenty-one years for women and eighteen years for men. *Id.* at 6.

This Article argues that Congress should incorporate a more comprehensive view of asset protection into federal retirement policy. Specifically, retirement policy objectives should serve as the benchmark for defining asset protection boundaries, thus placing the concept of asset protection in direct service to retirement policy goals. That benchmark should guide: (1) the grant of federally sanctioned asset protection within the retirement plan setting; and (2) the denial of such protection in the context of more traditional trust devices that do not further any discernable federal purpose.

Part II begins the development of these arguments with an explanation of the association between the availability of asset protection for retirement plans and the protections historically afforded to more traditional wealth management arrangements under state trust laws. Part III then details the particular policy considerations and implementing legislation that underlie the American approach to ensuring that citizens have adequate income during their postemployment years. The basic antipoverty objective of Social Security begins that consideration. One's attention quickly turns, however, to the more troublesome private pension and individual savings components of the system. Pensions and savings are more troublesome because those retirement plans help retirees maintain—at considerable taxpayer expense—preretirement standards of living that vary drastically across income levels and, in many settings, only loosely serve the stated goal of retirement income security.

Part IV explores the asset protection attributes of retirement plans, with a focus upon the legislative protections afforded retirement plan interests over the last quarter century. This exploration reveals that a lack of overt coordination between the legislative efforts that govern the intersection of asset protection and federal retirement policy have resulted in serious judicial dilemmas. As explained in Part IV, those interpretive dilemmas caused the modern rules of retirement plan asset protection to evolve in two very distinct progressions. Part IV characterizes and evaluates those progressions. Part IV reveals that an important third step in the evolution of retirement plan asset protection currently is underway. Specifically, Congress now believes that retirement plan asset protection should be more closely linked to a retirement plan's status as "tax-qualified."¹⁷ The federal laws that convey such status provide an incentive for funding future retirement through current savings, although the incentive is expensive and sometimes inequitably provided. Part V considers the implications of linking asset protection to the rules that embody that imperfect incentive. This endeavor ultimately fuels an examination of how, and why,

17. The term "tax-qualified" is explained *infra* note 120 and Part III.C.

asset protection might be more effectively tailored to foster the broader goal of retirement income security.

II. Protection Through Restrained Alienability: Context and Doctrine

Where a direct restraint on alienation protects a trust interest, the beneficiary retains the prospect of further enjoyment of her interest notwithstanding a thwarted creditor's efforts to reach that interest.¹⁸ The resulting prospect of continued enjoyment of otherwise sheltered property presents one of the more significant foundations for a long-running policy debate over asset protection.¹⁹ That debate found early life in traditional trust

18. See, e.g., IIA AUSTIN WAKEMAN SCOTT & WILLIAM FRANKLIN FRATCHER, *THE LAW OF TRUSTS* § 150 (4th ed. 1987) (distinguishing anti-alienation provisions from other trust protections by reference to the beneficiary's ability to continue to enjoy the trust property where protection is obtained through the anti-alienation route, versus other possible trust protections). The anti-alienation characterization reflects the fact that such provisions present a classic restraint on the ability to transfer an interest in property. Such restraints generally are deemed void, with the spendthrift trust provision being a noted exception to that outcome. See generally Gregory S. Alexander, *The Dead Hand and the Law of Trusts in the Nineteenth Century*, 37 STAN. L. REV. 1189 (1985) (discussing restraints on alienation). A "spendthrift trust" is most basically defined as a trust that is subject to a provision that states simply, for example, "that the interest of the beneficiary is inalienable and that creditors cannot reach the interest in satisfaction of their claims." See 1 RESTATEMENT (SECOND) OF TRUSTS § 155(1) (1959) (determining that a trust's terms can prevent a creditor from accessing a trust's assets). The spendthrift restraint might be included in the trust instrument as an expression of the trust settlor's intent that the beneficiary's interest be so restricted and thus protected. The provision might also apply, for example, by operation of some statute that deems the particular type of trust at issue to be subject to such a restriction. To be truly effective, such a provision must operate to preclude both voluntary alienation at the behest of the beneficiary, as well as involuntary alienation at the behest of the beneficiary's creditors. See *infra* note 21 (explaining the vulnerability of beneficial trust interests). The specific status of protected trusts in bankruptcy is developed more fully in Part IV.A.

19. The policy debate concerning the merits and demerits of spendthrift trusts is addressed in scores of scholarly articles. That debate will be referred to in this Article—although without wholesale repetition or revisitation—in order to provide context to the retirement policy debate. The arguments for and against recognition of spendthrift trust protections are summarized in GEORGE GLEASON BOGERT & GEORGE TAYLOR BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* § 223 (rev. 2d ed. 1992); RESTATEMENT (THIRD) OF TRUSTS § 58 cmt. a, reporter's note (Tentative Draft No. 2, 1999) [hereinafter DRAFT RESTATEMENT]; and IIA SCOTT & FRATCHER, *supra* note 18, § 152.

Concerning the ongoing nature of this policy debate, see, for example, DRAFT RESTATEMENT, *supra*, ch. 12 Introductory Note: "The philosophical and policy debate about spendthrift trusts . . . has continued for generations, still without consistent or enduring resolution" The debate recently was at the forefront in Mississippi, where the legislature stepped in to reverse a prior state supreme court decision that curtailed spendthrift trust protections. See *infra* note 37 (discussing the course of events that led to the Mississippi

doctrine, when the Supreme Court in 1875 endorsed the idea that an individual (the settlor) should be permitted to place assets in a trust, to designate a person (the beneficiary) as entitled to enjoy the benefits of the trust assets, and to preclude that beneficiary's creditors from forcing a transfer of the trust interest or assets in satisfaction of their claims.²⁰ State law enforcement of trust

legislation supporting spendthrift trust protection). The Ohio Supreme Court's 1991 reversal of its prior position denying the validity of spendthrift trusts also evidences the ongoing nature of this century-old debate. See *Scott v. Bank One Trust Co.*, 577 N.E.2d 1077, 1084 (Ohio 1991) (overruling *Sherrow v. Brookover*, 189 N.E.2d 90 (Ohio 1963)). This Article provides a rationale for resolving the spendthrift trust debate on the side of curtailed protection. This Article's rationale differs from many that have come before it because the argument is grounded in objectively discernable federal policy goals that contra-indicate the continued viability of this protective device.

20. The specific reference is to *Nichols v. Eaton*, 91 U.S. 716, 725 (1875), in which the Supreme Court opined "that [trust] property may . . . be enjoyed by . . . an individual without liability for his debts being attached as a necessary incident to such enjoyment . . ." The case presented a bankruptcy issue and the endorsement of protected trust interests was mere dictum regarding an area traditionally considered the province of state law. Noted commentators nevertheless have characterized *Nichols* as "the greatest single factor in the establishment of spendthrift trusts in the United States." ERWIN N. GRISWOLD, SPENDTHRIFT TRUSTS § 26(1) (2d ed. 1947); see also DRAFT RESTATEMENT, *supra* note 19, § 58 cmt. a, Reporter's Note (quoting Griswold on this point); Karen E. Boxx, *Gray's Ghost—A Conversation About the Onshore Trust*, 85 IOWA L. REV. 1195, 1197 (2000) ("As spendthrift trusts gained recognition at the turn of the nineteenth century, their primary foe, John Chipman Gray, acknowledged defeat without surrendering his objections." (footnote omitted)); Willard M. Bushman, *The (In)validity of Spendthrift Trusts*, 47 OR. L. REV. 304, 307 (1968) (pointing to *Nichols* as "the foundation upon which the American spendthrift-trust doctrine is built"); Anne S. Emanuel, *Spendthrift Trusts: It's Time to Codify the Compromise*, 72 NEB. L. REV. 179, 179 n.1 (1993) ("I date the [spendthrift trust] controversy from the dictum by Justice Miller in *Nichols v. Eaton* . . ."); Lawrence M. Friedman, *The Dynastic Trust*, 73 YALE L.J. 547, 582 (1964) ("The decisive cases validating the [spendthrift] clause fall into a relatively narrow time-span, beginning about 1880, following in rapid succession for about 25 years, then tapering off, since most jurisdictions had by then settled the major issue.").

Griswold goes on to note that shortly after the *Nichols* decision, influential text writers of the day had revised their works to embrace the *Nichols* dictum as law. GRISWOLD, *supra*, at § 30(4). In fact, the leading critic of the day proclaimed the *Nichols* decision a "startling novelty" and went so far as to conclude that the tide likely would have turned *against* the acceptability of such protected trusts had Justice Miller's arguments been levied with equal force in the negative. JOHN CHIPMAN GRAY, RESTRAINTS ON THE ALIENATION OF PROPERTY V (2d ed. 1895). With regard to subsequent decisions, see Stewart E. Sterk, *Asset Protection Trusts: Trust Law's Race to the Bottom?*, 85 CORNELL L. REV. 1035, 1042 n.46 (2000) ("Judicial enforcement of spendthrift trusts can be traced to two leading decisions." (citing *Nichols* and *Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882))). One should also note other dynamics of the legal, financial and social fabric of the day. See generally Alexander, *supra* note 18, at 1201–08 (discussing the *Nichols* decision in the broader context of restraints on alienation as evolved during the period 1875–1900); Friedman, *supra*, at 582–83 (discussing the broader economic and social climate of the day in relation to the development of the spendthrift trust doctrine). With regard to the specific definition of a "spendthrift trust," see *supra* note 18 and accompanying text.

provisions that facially purported to prohibit any transfer of a trust beneficiary's interest provided the direct path to this protected enjoyment.²¹ Although not generally recognized prior to the 1875 Supreme Court endorsement in *Nichols v. Eaton*, by the close of the nineteenth century this "anti-alienation" or "spendthrift" trust variant of asset protection was an established fixture in the United States legal framework.²²

Critiquing the resistance to this means of asset protection, one early commentator noted that "[i]t seems that it is not so much that the common law wants creditors paid [as a self-justifying proposition] . . . but that [the law] is opposed to having debtors refuse to pay creditors *and* still retain the property."²³ John Chipman Gray posited a more demonstrative statement of opposition to this form of asset protection in his oft-quoted nineteenth century treatise conclusion that "[t]he general introduction of spendthrift trusts would be to form a privileged class, who could indulge in every speculation . . . and yet . . . roll in wealth."²⁴ Gray's objection retains its vitality today when applied

21. Absent specific limitation, the beneficiary likely would have full power to transfer her beneficial rights and interests in the trust—including the right to receive distributions. For example, the beneficiary could transfer her right to receive distributions of income from the trust, but could not transfer any legal interest in the underlying trust property by virtue of which income is earned in support of such distributions. Thus, those rights could be taken away from the beneficiary, either at the beneficiary's doing or through involuntary transfer such as that occasioned by creditor requisition. The concept of asset protection is interjected when the arrangement is crafted such that both the beneficiary and the beneficiary's assignees or creditors are denied the ability to effect a transfer of the beneficiary's interest. The most direct means to this end is found where the interest is subjected to a direct restraint on alienability, as explained *supra* note 18. With respect to the distinction between direct and indirect restraints on alienation, see IIA SCOTT & FRATCHER, *supra* note 18, § 150.

As to the manner in which a creditor actually might liquidate or realize the value of a beneficiary's interest in a trust that *lacks* an enforceable spendthrift restraint, see EUGENE F. SCOLES ET AL., PROBLEMS AND MATERIALS ON DECEDENTS' ESTATES AND TRUSTS 627 (6th ed. 2000). For the same analysis in the specific context of a retirement plan interest, see *infra* note 243.

22. See the commentaries discussed *supra* note 20 regarding the enforceability of anti-alienation provisions around the turn of the nineteenth century.

23. George P. Costigan Jr., *Those Protective Trusts Which Are Miscalled "Spendthrift Trusts" Reexamined*, 22 CAL. L. REV. 471, 480 (1934) (emphasis added).

24. GRAY, *supra* note 20, § 262. As another early commentator put it:

[T]he need of the protection for the [beneficiary] was not stressed in the spendthrift trust cases, but the supposed freedom of the donor to protect his own acquired property from the creditors of his donee was emphasized, with the result that . . . [spendthrift trust settlors] . . . were permitted to provide for the beneficiaries of such trusts . . . incomes of any amount—no matter how large—free from the claims of the beneficiaries' creditors [And regardless of] the need of the beneficiaries for protection

Costigan, *supra* note 23, at 483.

to a traditional trust. In that context, the availability of asset protection generally has become disassociated from any required showing of particular need or other beneficiary infirmity that might justify the protection as anything other than a tool of wealth preservation.²⁵ Moreover, the primary historical defense of such protection has little to do with furthering broader social policy objectives like providing a fresh start to debtors or ensuring that an elderly person has some measure of postemployment financial stability.²⁶ Instead, early proponents of spendthrift trust asset protection asserted most forcefully that a donor should be free to dispose of her property for the benefit of a specified individual, without the courts usurping that freedom by including the individual's creditors in the class of persons entitled to benefit from the donor's largess.²⁷

A. *Expanding the Scope of an Ongoing Debate*

Interestingly, it was also in 1875 that corporate America established the first private retirement plan.²⁸ At the time, little connection appeared to exist between this milestone and the emerging acceptance of the "traditional" spendthrift trust asset protection vehicle. Yet, almost a century later, in 1974, Congress undeniably connected the two mediums by enacting sweeping changes to federal pension laws that subjected scores of retirement plan interests to the same anti-alienation language that dominated the realm of the

25. See *supra* note 20 and accompanying text (tracing this disassociation to the decisions embracing spendthrift protections in the late 1800s and the arguments posited in support of this view). A primary argument of the day was based upon respect for a trust settlor's freedom of disposition, as discussed in the text accompanying *infra* notes 26–27.

26. See *infra* Part IV.A.2 (regarding the bankruptcy policy of promoting a debtor's fresh start). The "fresh start" moniker denotes the idea that no debtor should emerge from insolvency destitute and on the public dole, but rather the debtor should be able to preserve some base of resources sufficient to allow the debtor to "get back on her feet." *Id.* As to spendthrift protections furthering such ideas, see, for example, William T. Vukowich, *Debtors' Exemption Rights*, 62 GEO. L.J. 779, 790–91 (1974) (contrasting bankruptcy exemption policies with policies underlying recognition of spendthrift restraints). The postemployment financial security of former wage-earners is considered in Part III.

27. See, e.g., *Nichols v. Eaton*, 91 U.S. 716, 718 (1875) (stating this argument); *Broadway Nat'l Bank v. Adams*, 133 Mass. 170, 173 (1882) (same); *Scott v. Bank One Trust Co.*, 577 N.E.2d 1077, 1082 (Ohio 1991) (citing the freedom of disposition argument proffered in *Nichols* as "most persuasive" in reasoning that prior Ohio precedent rejecting spendthrift trusts should be reversed).

28. See ALICIA H. MUNNELL, *THE ECONOMICS OF PRIVATE PENSIONS* 8 (1982) (discussing this history). The plan was established by American Express Corporation. *Id.*

traditional spendthrift trust.²⁹ Indeed, for many years after Congress passed this new pension legislation, traditional spendthrift trust principles served as the benchmark for resolving matters of asset protection for many retirement plan interests.³⁰ The lack of congressional guidance accompanying the federal anti-alienation provision, coupled with the seeming lack of coordination between the new retirement plan laws and the wholesale revisions to federal bankruptcy laws enacted a few years later,³¹ however, led to much disagreement in the academic commentary and in the federal courts.³² A focal point of that disagreement concerned the entitlement of a retirement plan participant to avail herself of the same protections clearly afforded to traditional spendthrift trust beneficiaries under federal bankruptcy laws.³³ Retirement plans that shared some similarities with the congressionally spendthrifted interests, but which were not subject to the 1974 federal spendthrift mandate, complicated the debate.³⁴

B. A Doctrinal Framework for Evaluation

Despite a rash of commentary and seemingly conclusive judicial decisions, the increasingly important concept of asset protection as it relates to federal retirement policy continues to present inconsistent and sometimes ill-conceived outcomes.³⁵ The resulting legal framework is disjointed and reflects a narrowly

29. See ERISA, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C. (labor provisions) and 26 U.S.C. (tax provisions)) (modifying federal pension laws). The anti-alienation provision is mandated at ERISA § 206(d)(1), 29 U.S.C. § 1056(d)(1) (2000), and also appears at 26 U.S.C. § 401(a)(13) (2000), as more fully discussed *infra* notes 103-28 and accompanying text. Title 26 of the United States Code is hereafter referred to as the Internal Revenue Code or I.R.C. With regard to equating the ERISA anti-alienation mandate to the language typically associated with traditional spendthrift trusts, see *supra* note 18 and *infra* note 109 and accompanying text.

30. See *infra* Part IV (focusing on the legislative protections for retirement plan interests since ERISA's enactment).

31. The reference is to the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C.).

32. These disagreements are discussed in detail beginning at *infra* Part IV.B of this Article.

33. Part IV.A discusses in detail this aspect of federal law.

34. See *infra* Part IV.B (addressing ERISA's effects on spendthrift trusts).

35. Post-ERISA evolutions in retirement plan asset protection are detailed *infra* Part IV.B. That evolution is affected by the Supreme Court decision in *Patterson v. Shumate*, 504 U.S. 753 (1992), discussed *infra* Part IV.B.2. With respect to the federal circuit court split that inspired *Shumate*, see generally STAFF OF JOINT COMM. ON TAX'N, 102D CONG., JCS-16-91, PRESENT LAW AND ISSUES RELATING TO THE TREATMENT OF QUALIFIED PENSION PLANS IN PERSONAL BANKRUPTCY 6-7 (Comm. Print 1991) [hereinafter JCS-16-91]. For commentary on

conceived patchwork of congressional pronouncements that appear to address asset protection as an afterthought, if at all. Quite simply, Congress has failed to account for the broader interaction across the multiple contexts in which contemporary asset protection is pursued. For example, an examination of the current asset protection environment reveals: (1) the emerging prominence of offshore and domestic asset protection trust devices for those seeking to create a protected base of assets for personal enjoyment;³⁶ (2) the codification and re-posturing of protections for more traditional spendthrift trusts historically used to protect assets given to third-party beneficiaries like children and grandchildren;³⁷ and (3) an increasing emphasis on asset protection for a vast array of retirement arrangements that purportedly further an individual's income security during retirement years.³⁸

the underlying issues across two decades, see generally, for example, Patricia E. Dilley, *Hidden in Plain View: The Pension Shield Against Creditors*, 74 IND. L.J. 355 (1999); Donna Litman, *Bankruptcy Status of "ERISA Qualified Pension Plans"—an Epilogue to Patterson v. Shumate*, 9 AM. BANKR. INST. L. REV. 637 (2001); Anthony Michael Sabino & John P. Clarke, *The Last Line of Defense: The New Test for Protecting Retirement Plans From Creditors in Bankruptcy Cases*, 48 ALA. L. REV. 613 (1997); Donna Litman Seiden, *Chapter 7 Cases: Do ERISA and the Bankruptcy Code Conflict as to Whether a Debtor's Interest in or Rights Under a Qualified Plan Can be Used to Pay Claims?*, Part I, 61 AM. BANKR. L.J. 219 (1987); Daniel Spitzer, Comment, *Contra Goff: Of Retirement Trusts and Bankruptcy Code § 541(c)(2)*, 32 UCLA L. REV. 1266 (1985); Laurence B. Wohl, *Pension and Bankruptcy Laws: A Clash of Social Policies*, 64 N.C. L. REV. 3 (1985); Lisa M. Smith, Note, *ERISA Qualified Pension Plans as Part of the Bankruptcy Estate After Patterson v. Shumate*, 21 CARDOZO L. REV. 2119 (2000).

36. See generally, e.g., Sterk, *supra* note 20 (discussing the implications of domestic asset protection trust legislation). That domestic trust legislation is addressed in this Article at *infra* notes 52–55 and the accompanying text.

37. See, e.g., UNIF. TRUST CODE §§ 501–07, 7C U.L.A. 174 (Supp. 2003) (codifying many common law rules pertaining to trust asset protection), available at <http://www.law.upenn.edu/bll/ulc/uta/utc00.pdf>; see also MISS. CODE ANN. § 91-9-503 (Supp. 2001) (codifying protection of certain trust interests, without exception for tort claimants, in the wake of a controversial Mississippi Supreme Court decision allowing tort creditors to reach spendthrift trust assets); Scheffel v. Krueger, 782 A.2d 410, 412–13 (N.H. 2001) (holding that a tort judgment debtor's interest in a spendthrift trust is protected under statute, and deeming public policy arguments based on the criminal nature of the beneficiary's sexual assault upon a minor plaintiff beyond the court's purview to consider); DRAFT RESTATEMENT, *supra* note 19, §§ 57–60 (providing a modern interpretation of conventional spendthrift trust protections). The noted Mississippi court decision came in *Sligh v. First Nat'l Bank*, 704 So. 2d 1020 (Miss. 1997). In *Sligh*, the state court opined that a trust beneficiary's gross negligence bordering on intentional conduct was a sufficient justification to override the discretionary-spendthrift nature of the trust at issue so as to permit the tort victim to satisfy his judgment against the trust beneficiary out of trust property. *Sligh*, 704 So. 2d at 1028. The Mississippi legislature subsequently disagreed. See MISS. CODE ANN. § 91-9-503 (codifying protection of certain trust beneficiary interests).

38. See, e.g., Peter Spero, *Impact of Bankruptcy Reform Legislation on Asset Protection*, 28 EST. PLAN. 291, 295 (2001) (discussing the impact of pending amendments to federal bankruptcy laws on retirement arrangements). That pending legislation is considered in detail *infra* notes 265–73 and accompanying text.

Focusing upon these three asset protection situations is helpful. The segmentation emphasizes differences in the origins of and purposes served by the protection in each context.³⁹ This segmentation also provides a construct for evaluating retirement plan asset protection concerns. More specifically, these three opportunities to shelter assets grew out of the "Traditional Model" of asset protection. Under the Traditional Model, applicable state law permits a trust settlor to create a creditor-protected trust *to be enjoyed by a third-party beneficiary*.⁴⁰ The "Self-Settled Model" differs from the Traditional Model. An individual settlor operating under the Self-Settled Model may, under applicable state or offshore jurisdictional law, establish and fund a creditor-protected trust *to be enjoyed by that funding individual settlor*.⁴¹ Finally, the "Federal Retirement Model" warrants independent consideration. Under the Federal Retirement Model, an individual, acting directly or through an employer, may establish and fund a tax-favored, creditor-protected trust or related arrangement *to be enjoyed by that individual, typically under the ambit of furthering such individual's financial security during retirement years*.⁴²

39. The separate identification of these three models crystallizes certain distinct rationales and implications of protecting assets from the reach of creditors. These "models" could perhaps more generously be called "paradigms" in that each implicates a particular set of rules. Alternatively, they could more practically be called simple "vehicles" through which assets might be held where protection from creditors is desired. One could quite readily call all three mere variations on the traditional spendthrift trust, but such simplistic analysis obscures the evolution of retirement plan asset protection as something unique and subject to its own set of concerns and rationales, the implications of which are precisely the point of this Article. As to other possible models of asset protection, perhaps the most obvious is "bankruptcy exemption planning." See generally Lawrence Ponoroff, *Exemption Limitations: A Tale of Two Solutions*, 71 AM. BANKR. L.J. 221, 227–33 (1997) ("Exemption planning" . . . entails the deliberate effort on the part of a financially beleaguered debtor to liquidate assets that are not exempt from the claims of general creditors and then use the proceeds . . . to purchase, make improvements upon, or pay down existing encumbrances on assets that are exempt . . .").

40. Recognition of the Traditional Model, as discussed *supra* notes 20–22 and accompanying text, inspired the policy debate described *supra* Part II.A.

41. As discussed in the text accompanying *infra* note 49, the Traditional Model denies protection where the trust settlor also is the beneficiary of the arrangement.

42. Although the trust form dominates arrangements in the employer-sponsored retirement plan context, retirement-associated vehicles like the Individual Retirement Arrangement (IRA)—which may or may not take the form of a trust and which may or may not be employer-sponsored—also factor into the broader model, though necessitating more discerning analysis. The retirement trust vehicle and the specific placement of IRAs, Keogh plans and similar arrangements within the context of the Federal Retirement Model are discussed more thoroughly in Parts III–V, and the distinctive features of those arrangements as they relate to the focus of this Article will not be overlooked. The conceptualization of the three models here is undertaken in furtherance of framing the larger analysis, and the boundaries of each model are made clear for such pursuits. In that regard, it is sufficient to note here that the bulk of employer-sponsored retirement plans necessarily embrace the trust form, and the Federal

Federal laws and policy affirmatively encourage the establishment of the tax-favored arrangements that comprise the Federal Retirement Model, and this encouragement serves as a particular source of distinction relative to the other models.⁴³

These asset protection models share the idea of beneficial property enjoyment coupled with some limitation or restraint upon the alienability of the beneficiary's interest.⁴⁴ "Beneficial enjoyment" denotes a person's equitable interest in a pool of assets—such as those held in a trust or retirement plan—by virtue of which distributions might be made to that beneficiary.⁴⁵ At least in the traditional trust setting, by definition the equitable nature of the beneficiary's interest implies that the beneficiary lacks any legal authority to transfer the *underlying pool of assets*.⁴⁶ Such authority instead resides with the person or entity (the trustee) charged with managing the property with the best interests of the beneficiary in mind.⁴⁷ From a practical standpoint, this distinction sometimes breaks down in the context of the Federal Retirement Model, because the retirement plan participant (i.e., the employee-beneficiary) may have meaningful access to the underlying funds by virtue of federal laws that regulate distributions from such plans.⁴⁸

Additional considerations affect the merits of asset protection within the Self-Settled Model. In particular, courts have long denied enforcement to anti-alienation provisions and other protections included in "self-settled" arrangements—those involving the same individual as both settlor and beneficiary.⁴⁹ Such self endowment is a bit too indicative of Gray's privileged

Retirement Model is intended to encompass not only those arrangements, but also alternative vehicles which similarly serve (in theory, at least) the retirement income security objective discussed in Part III.

43. The referenced federal policy and its implementation are the subject of *infra* Part III.

44. This generalization is qualified in detail *infra* Parts III and IV.

45. See *In re Barnes*, 264 B.R. 415, 432 (Bankr. E.D. Mich. 2001) (discussing essential characteristics of a trust relationship).

46. *Id.*

47. *Id.*

48. See *infra* note 216 regarding these federal laws. For recent commentary explaining, and to varying degrees, critiquing these federal laws, see generally, for example, Marcia Chadwick Holt, *New! The 2001 Proposed Regulations for Qualified Plans and IRAs*, TR. & EST., May 2001, at 20; Jay A. Soled & Bruce A. Wolk, *The Minimum Distribution Rules and Their Critical Role in Controlling the Floodgates of Qualified Plan Wealth*, 2000 B.Y.U. L. REV. 587; and Mark J. Warshawsky, *Further Reform of Minimum Distribution Requirements for Retirement Plans*, 91 TAX NOTES 297 (Apr. 9, 2001).

49. See, e.g., Sterk, *supra* note 20, at 1043 ("[E]ven more entrenched than spendthrift trust doctrine itself is the rule that a spendthrift provision for the settlor's own benefit is unenforceable." (footnote omitted)). In fact, the origins of this prohibition against self-settled

class,⁵⁰ and the retained interest falls short in appeal to the historical freedom of disposition justification for protection.⁵¹ In a clear but quite recent break from the historically discernable parameters of the Traditional Model, however, many jurisdictions now permit by statute a trust settlor to create, fund, and enjoy the benefits of a trust that is immune from the claims of the settlor-beneficiary's creditors.⁵² From a purely domestic perspective, this Self-Settled Model blossomed in 1997 when Alaska enacted domestically unprecedented legislation aimed at encouraging the creation of self-settled asset protection trusts.⁵³ Reflecting the pace of recent evolutions in asset protection thinking,

spendthrift trusts can be traced to at least 1487. See IIA SCOTT & FRATCHER, *supra* note 18, § 156 (tracing the origin of this rule to the 1487 Statute of King Henry VII, 3 Hen. 7, c.4 (1487) (Eng.), which voided conveyances in trust for the use of the transferor). See the text accompanying *supra* note 20 regarding the "settlor" as the individual funding a trust.

50. See *supra* note 24 and accompanying text (quoting Gray's assertion that widespread use of spendthrift trusts will result in the rise of a privileged class).

51. See *supra* notes 25–27 and accompanying text regarding the freedom of disposition argument. The argument fails in the self-settled context because the settlor also is the recipient of the beneficial trust interest, thus undermining the argument that there has been any meaningful disposition. See, e.g., Emanuel, *supra* note 20, at 190–91 (discussing this aspect of the freedom of disposition rationale).

52. See *infra* note 54 and accompanying text (discussing states' adoption of asset protection legislation). Self-funded, protected enjoyment would be the likely result with respect to an action controlled by the laws of one of these jurisdictions. Instances exist, however, in which a forum court may apply the laws of the state in which it sits and refuse to recognize the laws of a more protective jurisdiction, which purportedly govern the trust. See generally RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 270 (1971) (addressing the validity of a trust when the applicability of the laws of multiple jurisdictions is at issue); *Id.* § 273 (addressing the more specific question of whether a spendthrift provision restraining a beneficiary's ability to alienate an interest in the trust property will be given effect); BOGERT & BOGERT, *supra* note 19, §§ 291, 301 (identifying and avoiding conflict of law problems); V.A. SCOTT & FRATCHER, *supra* note 18, § 573 (discussing the effects of a judgment by a non-primary court in a different state). This would likely be the case, for example, when the laws of a jurisdiction designated by the settlor in the trust instrument would recognize self-settled protections but would offend the public policy of the forum state in which a legal action concerning the trust is brought. See 17A JAMES WM. MOORE ET AL., MOORE'S FEDERAL PRACTICE § 124.31(4)(c)(i) (3d ed. 1999) (noting that choice of law provisions will not be given effect when "[a]pplication of the law of the chosen state would be contrary to a fundamental policy of a state . . . that has a materially greater interest than the chosen state in the determination of the particular issue"). Determining the law that governed the effectiveness of self-settled protections was a pivotal issue in *Marine Midland Bank v. Portnoy* (*In re Portnoy*), 201 B.R. 685 (Bankr. S.D.N.Y. 1996), and in *Sattin v. Brooks* (*In re Brooks*), 217 B.R. 98 (Bankr. Conn. 1998). For discussion of these cases and the conflicts of law issues that arise in the context of self-settled asset protection trusts, see, for example, John K. Eason, *Home from the Islands: Domestic Asset Protection Trust Alternatives Impact Traditional Estate and Gift Tax Planning Considerations*, 52 FLA. L. REV. 41, 69–72 (2000); Sterk, *supra* note 20, at 1081–89.

53. ALASKA STAT. § 34.40.110 (Michie 2000). The Alaska legislature pursued this objective through statutory language that expressly permits a person to transfer property to an

Delaware, Nevada, and then Rhode Island quickly followed suit in adopting domestic APT legislation.⁵⁴ Such developments relate to federal retirement policy because in many instances commentators easily characterize the plans that comprise the Federal Retirement Model as self-settled, and sometimes judge the resulting protections accordingly.⁵⁵

C. *The Promise of Perspective*

The interaction between asset protection and federal retirement policy today presents a divided landscape. Specifically, certain retirement arrangements simply receive blanket asset protection without further inquiry. Other retirement arrangements, however, continue to receive careful scrutiny based upon criteria derived from analysis typically ascribed to the Traditional

Alaska-sitused trust and to provide in the trust agreement that the beneficiaries' trust interests—including specifically the interest of the settlor as beneficiary—may not be voluntarily or involuntarily alienated. *Id.* The term "situs" generally refers to the place at which a thing—in this case, a trust—is deemed to be located for legal purposes. BLACK'S LAW DICTIONARY 1392 (7th ed. 1999).

54. DEL. CODE ANN. tit. 12, §§ 3570–3573 (2001); NEV. REV. STAT. §§ 166.040–050 (2001); R.I. GEN. LAWS §§ 18-9.2-1–18-9.2-7 (Supp. 1999). These subsequent laws bear substantial similarities to the Alaska model in both form and substance. A mirror image of the Alaska legislation was proposed but not acted upon in the 1999 session of the Texas House. H.B. 1553, 76th Leg., Reg. Sess. (Tex. 1999) (introduced Feb. 17, 1999), <http://www.capitol.state.tx.us> (last visited Oct. 11, 2003) (on file with the Washington and Lee Law Review). It is sometimes said that Missouri and Colorado might be self-settled asset protection trust jurisdictions, but this claim is questionable. See MO. ANN. STAT. § 456.080 (West 1992) (providing what appears to be limited asset protection for self-settled spendthrift trusts, dating back to 1983); A. JAMES CASNER & JEFFREY N. PENNELL, 1 ESTATE PLANNING § 4.1.4 n.23 (6th ed. Supp. 2002) (discussing COLO. REV. STAT. § 38-10-111). The pertinent legislation in Missouri is of debatable legal and practical impact in the context of the Self-Settled Model, particularly in light of the domestic asset protection trust movement so clearly initiated by Alaska's 1997 adoption of comprehensive asset protection trust legislation. For an equally equivocal assessment of the Missouri statute, see Boxx, *supra* note 20, at 1203 n.30 ("Missouri may also recognize self-settled trusts as enforceable to some degree.").

55. See the discussion of this issue *infra* Part IV.B. For early, pre-ERISA recognition of this issue, see, for example, Friedman, *supra* note 20, at 582 (noting that Social Security and private pension plans create a creditor-protected fund, but then questioning the soundness of this result in light of the self-settled nature of the arrangement); Note, *Legal Problems of Private Pension Plans*, 70 HARV. L. REV. 490, 499 (1957) (discussing the self-settled nature of private pensions and the corresponding rule that spendthrift provisions are not effective as to self-settled trusts). Where employer contributions are involved, the fact that they are made in consideration of services provided by the employee and as an alternative to cash paid directly to the employee renders these arrangements subject to consideration as self-settled, despite the fact that the funds never actually passed through the employee-settlor's hands. For further exposition of this issue, see *infra* notes 212–13 and accompanying text.

and Self-Settled Models or to bankruptcy exemption laws more generally.⁵⁶ This Article seeks a broader perspective from which to evaluate the relationship between the noted asset protection models as they affect the attainment of federal retirement policy goals. The fundamental policies and implementing mechanisms that define those goals are the subject of Part III.

III. The Policy Underpinnings of the Federal Retirement Model

The idea that workers should have adequate income to provide for their needs during their postemployment years is central to federal retirement policy.⁵⁷ While the determination of how to define, achieve, and motivate persons toward this objective continues to garner much debate, the broad framework in the United States for pursuing the goal of retirement income security is a tripartite system often analogized to a three-legged stool. The three "legs" are Social Security, private employer-sponsored pension plans, and personal savings.⁵⁸ Each leg or aspect of the system represents one of the primary sources of income available to an individual after retirement, when income from wage earnings presumptively has ceased as a primary source of

56. This assertion is explored in detail *infra* Part IV. Regarding bankruptcy exemption laws specifically, see *infra* Part IV.A.2.

57. See generally STAFF OF JOINT COMM. ON TAX'N, 106TH CONG., JCX-16-99, OVERVIEW OF PRESENT-LAW TAX RULES AND ISSUES RELATING TO EMPLOYER-SPONSORED RETIREMENT PLANS 20 (Comm. Print 1999) [hereinafter JCX-16-99] ("Retirement income policy has as its goal the delivery of adequate retirement benefits to the broadest possible class of workers."); NAT'L COMM'N ON RET. POLICY, THE 21ST CENTURY RETIREMENT SECURITY PLAN (1999) [hereinafter 21ST CENTURY] (addressing the problems of the current system and proposing a solution), available at <http://www.csis.org/retire/NCRPFinal.pdf>; MUNNELL, *supra* note 28, at 7 (noting that the Social Security and private pension systems "are alternative ways to accomplish the same goal—namely, providing an adequate retirement income").

58. With respect to the three-legged stool analogy, see Nancy J. Altman, *Rethinking Retirement Income Policies: Nondiscrimination, Integration, and the Quest for Worker Security*, 42 TAX L. REV. 435, 501–02 (1987) (discussing this analogy); Michael J. Graetz, *The Troubled Marriage of Retirement Security and Tax Policies*, 135 U. PENN. L. REV. 851, 852–53 (1987) ("Commentators typically describe a tripartite system that enables and encourages the provision of income security for individuals in the years following retirement . . ."). Sometimes the elements are cast differently. See, e.g., PRESIDENT'S COMM'N ON PENSION POLICY, COMING OF AGE: TOWARDS A NATIONAL RETIREMENT INCOME POLICY 11–13 (1981) [hereinafter COMING OF AGE] (noting three-legged stool components as described herein, but also discussing additional aspects of public assistance); PENSIONS AND THE ECONOMY xii (Zvi Bodie & Alicia H. Munnell eds., 1992) (describing "a three-tiered system of retirement income maintenance" comprised of: (1) public welfare programs like SSI; (2) mandatory public programs like Social Security; and (3) "private provisions for retirement, which include individual saving as well as supplementary employer-sponsored pension plans").

support.⁵⁹ The tri-part system reflects the utilization of "a full spectrum of policy initiatives" to achieve this objective: (1) the broad public federal program that is Social Security; (2) private savings, which represent "an individualistic program dependent principally upon . . . self-reliance",⁶⁰ and (3) employer-sponsored pension plans, which most often involve the meshing of federal tax incentives, employer sponsorship, and voluntary employee participation.⁶¹

Conceptually, commentators and policymakers evaluate the attainment of this retirement income security objective by reference to two related criteria: (1) ensuring a basic standard of living upon retirement; and (2) facilitating some added degree of lifestyle maintenance upon retirement.⁶² The three legs of the U.S. retirement system work in conjunction to affect this broad policy objective, as considered in light of the referenced criteria, by providing a means of replacing preretirement wages during the retirement years.⁶³ Employer-

59. JCX-16-99, *supra* note 57, at 17.

60. Graetz, *supra* note 58, at 854.

61. See *id.* (identifying employer pension plans as the balance between the two extremes of a broad federal program and private action).

62. See, e.g., MUNNELL, *supra* note 28, at 19–28 ("Once a minimum level of income support is assured, a replacement rate—the ratio of benefits to preretirement earnings—is actually a more appropriate criterion against which to assess wage-related benefit programs."); 21ST CENTURY, *supra* note 57, at 25 (listing among its guiding principles for national retirement policy the ideas of a retirement income floor coupled with initiatives to facilitate additional retirement income above such a floor); STEVEN A. SASS, THE PROMISE OF PRIVATE PENSIONS 111 (1997) (discussing dual roles of Social Security as providing retirement income at a floor level, with private pensions providing a supplement thereto); Altman, *supra* note 58, at 501 ("[T]he promise of retirement is illusory if the retirement income is inadequate."); Graetz, *supra* note 58, at 855 (noting "basic adequacy of income" and "lifestyle maintenance" components of retirement policy); Wohl, *supra* note 35, at 36 (noting that Congress felt something more than a bare retirement income floor was necessary).

63. See STAFF OF JOINT COMM. ON TAX'N, 104TH CONG., JCS-3-95, DESCRIPTION AND ANALYSIS OF TAX PROPOSALS RELATING TO INDIVIDUAL SAVINGS 9 (Comm. Print 1995) [hereinafter JCS-3-95] (determining that numerically, "[t]he adequacy of retirement income is commonly measured by the replacement rate, that is, the ratio of retirement income to income during working years"), available at <http://www.house.gov/jct/s-3-95.pdf>. It is generally acknowledged, however, that a replacement of 100% of preretirement earnings is neither necessary nor realistically attainable. *Id.* A specific percentage replacement as numerically indicative of successful accomplishment of the goal is elusive. See, e.g., MUNNELL, *supra* note 28, at 23 (estimating that retirees need between 50% to 80% of preretirement income to maintain their standard of living); 21ST CENTURY, *supra* note 57, at 18 (indicating that a 60% to 80% wage replacement would be needed for most people to maintain their preretirement standard of living); Altman, *supra* note 58, at 495–96 (noting that the precise percentage varies by worker, and that full wage replacement is probably not needed, and then assuming 80% replacement would indicate success); Graetz, *supra* note 58, at 856 n.9 (noting that retirement security objective would be ideally achieved where 100% of preretirement earnings are replaced). This narrow conception, however, ignores other public policy concerns such as

sponsored pension plans further this objective by "bridging the public anti-poverty/basic income adequacy function of Social Security and the private lifestyle maintenance function of individual savings" ⁶⁴ Understanding the Social Security system is, therefore, the first step to understanding the broader issue of retirement income security.

A. Social Security

The benefits provided to former wage earners and their survivors through the Social Security system represent the most basic source of postretirement income, and the first "leg" of the United States' tri-part retirement framework. ⁶⁵ Since its inception in 1935, Social Security has reflected the idea of securing a "floor" level of income during retirement. This idea is based upon the notion that some degree of social insurance is needed to stave off poverty at retirement when a worker typically forfeits income earned through regular wages. ⁶⁶ One

health insurance coverage or poverty law generally, as well as issues that arise when 100% wage replacement still leaves some individuals with income below some standard delineating poverty. *Id.*

64. Graetz, *supra* note 58, at 858.

65. See COMING OF AGE, *supra* note 58, at 11 (stating that Social Security grew out of an increasing perception, fostered by the Great Depression, that the federal government had a role to play in providing economic security to the elderly and concluding that Social Security now represents a broad-based public mechanism furthering the pursuit of that objective); U.S. GEN. ACCOUNTING OFFICE, HEHS-98-33, SOCIAL SECURITY: DIFFERENT APPROACHES FOR ADDRESSING PROGRAM SOLVENCY 24 (1998) [hereinafter PROGRAM SOLVENCY] (same). The Social Security system has several aspects. The system includes the provision of insurance benefits for old-age/retirement, survivors and family members of covered workers, and for disability and hospital care. Viewed from the standpoint of the payroll taxes which provide the bulk of its funding, *infra* note 71, the system breaks down into two major components: (1) the Old Age, Survivors and Disability Insurance (OASDI) component; and (2) the Health Insurance (HI) or Medicare component. See generally SOCIAL SECURITY ADMINISTRATION, ANNUAL REPORT 1-2 (2002) [hereinafter SSA ANNUAL REPORT], available at <http://www.ssa.gov/OACT/TR/TR02/tr02.pdf> (last visited Oct. 9, 2003) (on file with the Washington and Lee Law Review); SOCIAL SECURITY ADMINISTRATION, PUBLICATION NO. 05-10006 (2002), available at <http://www.ssa.gov/pubs/10006.html> (last visited Oct. 9, 2003) (on file with the Washington and Lee Law Review). "The . . . ('OASI') program provides benefits for retired workers and their spouses and children and to survivors of deceased workers. The Disability Insurance ('DI') program provides benefits for disabled workers and their spouses and children and pays for rehabilitation services for the disabled." Kathryn L. Moore, *Redistribution Under a Partially Privatized Social Security System*, 64 BROOK. L. REV. 969, 969 n.1 (1998). For purposes of this Article, "Social Security" means the OASDI aspect of the Social Security system. See, e.g., PROGRAM SOLVENCY, *supra*, at 2 n.1 (making a similar simplification); Karen C. Burke & Grayson M.P. McCouch, *Women, Fairness, and Social Security*, 82 IOWA L. REV. 1209, 1209 n.1 (same); Moore, *supra*, at 969 n.1 (same).

66. See MUNNELL, *supra* note 28, at 13 ("With the Social Security Act of 1935 the federal

must keep in mind that, for many workers earning a relatively low wage during their working years and lacking an independent source of accumulated wealth to finance their retirement lifestyles, Social Security retirement benefits provide a base level of income that is both a shield against impoverishment and the sole means of maintaining a semblance of their preretirement standard of living.⁶⁷ While the sufficiency of Social Security in this regard is debatable, the stated role is clear enough, and Americans widely regard the program as being successful in the strict sense of curtailing poverty among the aged.⁶⁸

It would be inaccurate, however, to characterize the program as a form of publicly financed social welfare. In fact, commentators sometimes describe the base level of retirement income promised through Social Security as an "earned

government assumed responsibility for maintaining a floor of income protection for the retired elderly."); Burke & McCouch, *supra* note 65, at 1211 (describing the Social Security system as a hybrid one, consisting of elements of a private insurance program and a social welfare program); Patricia E. Dilley, *The Evolution of Entitlement: Retirement Income and the Problems of Integrating Private Pensions and Social Security*, 30 LOY. L.A. L. REV. 1063, 1083 (1997) ("The income redistribution provided in the Social Security benefit formula seeks to slow the decline into poverty of elderly persons who can no longer work and improve their own financial condition."). Dilley notes that the purposes underlying Social Security are both "prophylactic" and prospective, in that the program permitted work-force management through the inducement of voluntary retirement at a specified age. *Id.* at 1107, 1133; see also COMING OF AGE, *supra* note 58, at 13 ("Social security is designed to provide a floor of income protection to retired and disabled workers and their families."). The referenced "floor" must be understood as not fixed across all workers, because the benefits paid to a particular retiree actually are calculated on a case-specific basis by reference to the retiree's average career earnings. See 21ST CENTURY, *supra* note 57, at 36–37 (simplifying Social Security benefit calculation to a three-step process); Altman, *supra* note 58, at 476–78 (discussing the mechanics of the determination of Social Security benefits). Average career earnings as used here include only those earnings up to the Social Security wage base, which in 2003 means the first \$87,000 of wage earnings. See *infra* note 74 (stating the wage ceiling). Earnings above this amount are neither subject to the FICA tax nor counted as part of a worker's average career earnings for benefit level calculation purposes. With respect to this floor concept, Social Security benefit levels are said to reflect "an implicit social judgment concerning the minimum amounts of income that workers should receive at retirement." Altman, *supra* note 58, at 494.

67. See PROGRAM SOLVENCY, *supra* note 65, at 12 (stating that Social Security provides over 40% of all income for persons aged sixty-five and older, with over 60% of this group looking to Social Security for at least half of their income). As to the balance of income sources among this group, pensions and annuities provide 20%, personal assets provide 20%, and post-retirement earnings comprise 18% of income. Sharon A. DeVaney & Yi-Wen Chien, *A Model of Savings Behavior and the Amount Saved in Retirement Accounts*, J. FIN. SERV. PROF., Mar. 2001, at 72, 72. The distribution among income groups is more telling, however, as in 1998 the lowest income quintile group received almost 90% of income from Social Security, whereas the figure dropped below 20% for the highest quintile group. *Id.* at 73.

68. See, e.g., PROGRAM SOLVENCY, *supra* note 65, at 78 ("The program has been highly effective at reducing the incidence of poverty among the elderly . . ."). With regard to the adequacy of the program and the need for supplemental sources of income after retirement, see *infra* notes 84–87 and accompanying text.

entitlement" that ensures not so much a specific level of benefits, but rather a source to which covered individuals may look for payment of benefits.⁶⁹ Participation is mandatory for most workers,⁷⁰ and the primary funding mechanism for Social Security is the "payroll tax" imposed upon workers, their employers, and the self-employed.⁷¹

69. See Burke & McCouch, *supra* note 65, at 1213 (discussing the "widely-held perception" of Social Security as an "earned right," but also discounting that perception as becoming more symbolic than real as the redistributive aspect of Social Security has grown); Dilley, *supra* note 66, at 1107-08 ("The entire structure of retirement income sources in the United States is based on individually-earned entitlements . . .").

70. See EMPLOYEE BENEFIT RESEARCH INST., FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS 16 (5th ed. 1997) [hereinafter FUNDAMENTALS] (asserting that workers populating approximately 95% of wage-paying jobs are subject to the Social Security system). Approximately forty-four million people currently receive Social Security benefits, financed primarily by payroll taxes collected from 147 million current workers. PROGRAM SOLVENCY, *supra* note 65, at 12.

71. See I.R.C. §§ 3101(a)-(b), 3111(a)-(b) (2000) (setting the "payroll tax" liability for employees and employers to finance old-age and survivors insurance and disability insurance benefits); 42 U.S.C. § 430 (2000) (providing for the determination of the Social Security contribution and benefit base); SSA ANNUAL REPORT, *supra* note 65, at 5 (reporting that in 2001 86% of the income of the OSAI, DI, and OSADI trust fund consisted of taxes paid by employees and employers on earnings covered by social security). Payroll taxes account for over 90% of the program's funding, with the balance being derived from interest earned on the surplus fund assets and taxes imposed on Social Security benefits paid to higher income beneficiaries. See I.R.C. § 86 (including Social Security benefits in taxable gross income if the sum of a taxpayer's modified adjusted gross income and one-half of Social Security benefits received exceeds a base amount); PROGRAM SOLVENCY, *supra* note 65, at 12-13 (reporting that in 1997 the Social Security program's revenues consisted of about 90% from payroll taxes, about 1.7% from income tax on Social Security benefits, and about 10% from interest on trust fund assets). The funding occurs on a "pay-as-you-go" basis, meaning generally that the Social Security trust fund—from which current benefits are paid to today's retirees—is financed through current payroll tax collections from today's workers. See generally 21ST CENTURY, *supra* note 57, at 8 (discussing impending Social Security shortfalls and possibilities for reform); PROGRAM SOLVENCY, *supra* note 65, at 15-20 (discussing pay-as-you-go financing and impending shortfalls implicated by changing demographics which indicate a reduction over the next several decades in current workers relative to elderly benefit recipients).

The funds collected often are referred to as comprising the "Social Security trust fund." In reality there is neither a fund nor a trust, though the analogy is apt in the sense that employees effectively are beneficiaries seeking to realize upon an interest administered by the federal government as trustee. Actually, the "massive account into which the annual [Social Security tax collections in excess of current benefits owed] are ostensibly deposited exists largely as a budgetary artifice instead of a pool of actual assets." *Id.* at 13. This "budgetary artifice" basically consists of a series of government obligations backed by the promise to tax workers in the future such that, upon current workers' retirement, adequate benefits might be paid. See *id.* at 13-15 (discussing pending shortfalls in Social Security funding as baby boomers retire and fewer workers remain to support the pay-as-you-go funding of Social Security); see also Allan Sloan, *The Social Security Crackup*, NEWSWEEK, July 3, 2000, at 18 (presenting a similar, although less technical, analysis of the trust fund "myth" and the pay-as-you-go nature of the system).

From an equity standpoint, although current payroll taxes are proportional in that the wages of all covered workers are taxed at the same flat rate of 6.2%,⁷² the burden of this funding mechanism is regressive in that it often requires lower wage earners to contribute a greater percentage of their earnings towards the payment of the tax than do higher wage earners.⁷³ Specifically, regressivity results because the first dollar of a worker's wages is subject to the tax at the flat rate, but once wages for a given year reach a certain dollar amount, all earnings above this wage ceiling are exempt from the tax.⁷⁴

72. The total FICA tax rate is actually 15.3%, of which half (or taxes attributable to a tax rate of 7.65%) are paid by the employer in the case of individuals who are not self-employed. See SOC. SECURITY & MEDICARE BD. OF TRS., SOC. SECURITY ADMIN., STATUS OF THE SOCIAL SECURITY AND MEDICARE PROGRAM: A SUMMARY OF THE 2003 ANNUAL REPORTS 2 (2003) (calculating the total FICA tax rate), at <http://www.ssa.gov/OACT/TRSUM/tr03summary.pdf> (last visited Nov. 7, 2003) (on file with the Washington and Lee Law Review). Of the worker's contribution, the taxes above the 6.2% rate go towards funding Hospital Insurance popularly known as Medicare. See *id.* at 2 (stating that the 2003 tax that funds Medicare is set at 6.2% for 2003); see also RICHARD A. WESTIN, WG&L TAX DICTIONARY 556 (2002) (defining "proportional tax" as "a tax which takes the same proportion of each taxpayer's income, often called a 'flat tax'").

73. See Joseph Bankman, *Tax Policy and Retirement Income: Are Pension Plan Anti-Discrimination Provisions Desirable?*, 55 U. CHI. L. REV. 790, 827 (1988) (stating that "[s]ocial security funds are collected in a regressive fashion . . ."); Graetz, *supra* note 58, at 864–65 (describing the Social Security tax burden as regressive because the payroll tax does not provide an exemption for wages that fall below a certain level but does contain a maximum level of wages that are subject to the tax).

74. For 2003, that ceiling is \$87,000, and wage earners will pay FICA taxes up to that amount at a rate of 6.2% towards the OASDI component of Social Security. See SOCIAL SECURITY ONLINE, OASDI CONTRIBUTION AND BENEFIT BASE (explaining that the 2003 contribution and benefit base has been set at \$87,000 and that the OASDI tax rate is set at 6.2% for both employees and employers), at <http://www.ssa.gov/OACT/COLA/CBB.html> (last visited Oct. 9, 2003) (on file with the Washington and Lee Law Review). With respect to regressivity in the funding mechanism for Social Security, consider that a worker having wages of \$50,000 in 2003 will pay FICA taxes on all wages earned for a total tax liability attributable to Social Security OASDI benefits of \$3,100, or 6.2% of her wages. In contrast, a worker having wages of \$200,000 in 2003 would pay FICA taxes on only the first \$87,000 of wages (i.e., only wages up to the 2003 wage ceiling amount are taxed), resulting in an OASDI tax liability of \$5,394—which although greater in amount, represents only 2.7% of such worker's wages. For more on this regressivity analysis, see Graetz, *supra* note 58, at 864–65, noting that the "fundamental problem" with the payroll tax lies in the upper and lower bounds of the wages subject to taxation. In evaluating the true magnitude of the regressivity, it should be kept in mind that "[e]conomists generally agree that both the employers' and the employees' shares of Social Security taxes are borne by employees in the form of reduced wages." Graetz, *supra* note 58, at 867; see *supra* note 72 (regarding the employer versus employee share of the tax); see also STEPHEN G. UTZ, TAX POLICY: AN INTRODUCTION AND SURVEY OF THE PRINCIPAL DEBATES 20–24 (1993) (discussing the idea of who bears the "incidence" of a tax, which may ultimately be someone other than the party nominally required to pay the tax). A relatively straightforward approach to mitigating this negative aspect of Social Security funding would be to repeal the wage ceiling such that all wages of higher income workers are subject to the tax, while

The progressive nature of the Social Security retirement benefit structure, however, mitigates the regressivity in the Social Security funding mechanism.⁷⁵ First, the formula for calculating benefit payments considers only that portion of a worker's average annual earnings that were subject to the payroll tax each year.⁷⁶ Higher wage earners therefore get no credit in the benefits formula for wages earned in excess of the applicable ceilings during their working lives. Second, the rate at which benefits are paid decreases as the amount of average annual covered wages increases.⁷⁷ The combination of these two factors results in Social Security replacing a lower percentage of higher lifetime preretirement wage earners' wages than lower lifetime wage earners. Stated differently, the benefits paid to former lower wage earners upon retirement generally should replace a greater percentage of their preretirement wages than the benefits paid to former high wage earners.⁷⁸ Consequently, commentators acknowledge this benefits structure as both progressive and positively redistributive.⁷⁹ In less

correspondingly imposing a wage floor below which the tax would not be imposed. See Graetz, *supra* note 58, at 864–74 (advocating this approach).

75. See ALAN L. GUSTMAN & THOMAS L. STEINMEIER, HOW EFFECTIVE IS REDISTRIBUTION UNDER THE SOCIAL SECURITY BENEFIT FORMULA? 1 (Nat'l Bureau of Econ. Research, Working Paper No. 7597, 2000) [hereinafter NBER No. 7597] (describing the Social Security benefit formula as progressive, replacing a higher share of earnings for individuals with lower incomes), available at <http://www.nber.org/papers/w7597>.

76. See SOC. SECURITY ADMIN., SOCIAL SECURITY: HOW YOUR BENEFITS ARE CALCULATED 1–2 (2003) (instructing that actual earnings, but not more than a maximum amount, are to be entered into the calculation of estimated retirement benefits), at <http://www.ssa.gov/pubs/10070.pdf> (last visited Nov. 7, 2003) (on file with the Washington and Lee Law Review); *supra* note 74 and accompanying text (regarding the wage ceiling). The rate considers the worker's earnings over the worker's thirty-five years of highest earnings. See PROGRAM SOLVENCY, *supra* note 65, at 13–15 (stating that benefits are currently calculated using the thirty-five years of highest earnings instead of total lifetime earnings).

77. For example, benefits recently were paid at the rate of 90% of the first \$6,372 of average annual earnings, 32% of the next \$32,052, and 15% of the excess earnings. See NBER No. 7597, *supra* note 75, at 5 (describing how the Social Security benefit formula works in general). These are the actual figures for the year 2000, when the FICA wage ceiling stood at \$76,200. See *id.* (providing the specific benefits formula for the year 2000). It also could be noted that a special minimum benefit is provided for certain workers having an adequate work history, but low average wages. See 42 U.S.C. § 415(a)(1)(C) (2000) (providing a minimum primary insurance amount of \$11.50 multiplied by the individual's years of coverage in excess of ten); Moore, *supra* note 65, at 972–73 (discussing this aspect of Social Security in terms of social adequacy).

78. See, e.g., Burke & McCouch, *supra* note 65, at 1212 (“[A] progressive formula . . . ensures that the ‘replacement rate’—the ratio of benefits to preretirement wages—varies inversely with the level of preretirement wages. High earners receive larger benefits in absolute terms, while low earners receive a larger percentage of their preretirement wages.” (footnotes omitted)).

79. See NBER No. 7597, *supra* note 75, at 5–6 (describing the calculation of Social Security benefits and stating that by applying a progressive formula, benefits are redistributed to

relative terms, Social Security retirement benefits constitute the major source of income for two-thirds of Social Security beneficiaries, and the only source of income for one-fifth of beneficiaries.⁸⁰ This fact emphasizes the important role such benefits play for a substantial segment of the former working population.

Given these realities and the base income maintenance objective at issue, it is not surprising that creditors of a worker covered by Social Security are precluded from collecting on their claims out of the worker's Social Security "entitlement."⁸¹ Despite the individual equity aspect of Social Security—which suggests that these promised "government" benefits are in fact calculated by reference to the recipient's own earnings history and thus could be characterized as being in the nature of a self-settled entitlement—this legislatively-granted protection has generated neither serious debate nor objection. In light of the progressive nature of the Social Security benefits structure and the status of persons most dependent upon such benefits, the protection at issue generally does not present significant equity concerns. The misnomer that would be "Social Security wealth protection," coupled with the poverty and resulting public burden that could result should such benefits be subjected to creditor claims, further evinces the lack of any significant overriding equity or other objection to the protection of such benefits from the claims of a worker's creditors.⁸² While the characterization in this Article of the Federal Retirement Model is most concerned with the tax-favored vehicles associated with private pensions and personal savings, a simplistic view (though a mischaracterization on some fronts) might posit an individual's Social Security entitlement as a beneficial interest in the Social Security trust fund, decisively shielded from creditor claims by virtue of the congressional

individuals with low covered earnings over their lifetimes); Burke & McCouch, *supra* note 65, at 1213 ("Social security has become massively redistributive . . ."); Graetz, *supra* note 58, at 872 (describing the first fifty years of Social Security as "a very successful redistributive program").

80. 21ST CENTURY, *supra* note 57, at 16; see also *supra* note 67 (discussing the balance of income for persons aged sixty-five and older).

81. See 42 U.S.C. § 407(a) (providing that no portion of an individual's Social Security benefits shall be subject to levy, attachment, garnishment, bankruptcy law or any other legal process); *Philpott v. Essex County Welfare Bd.*, 409 U.S. 413, 416–17 (1973) (finding that 42 U.S.C. § 407 bars all claims, including claims made by a state, against an individual's Social Security benefits).

82. *But see, e.g.,* RICHARD A. IPPOLITO, PENSION PLANS AND EMPLOYEE PERFORMANCE 62–74 (1997) (discussing the Social Security "wealth effect," which some commentators posit as historically having motivated earlier retirement decisions through provision of greater than expected benefits).

conclusion that the purpose and policies underlying that interest outweigh any concern for creditors.⁸³

The point here, however, is not to deconstruct that characterization. The purpose of this Article is to explain the Social Security model, its anti-poverty function, and its asset protection component as aspects of the larger retirement income security objective. This discussion serves as a precursor to more difficult inquiries relating to asset protection for the remaining legs of the triadic retirement income security stool. In that vein, one must note that Social Security benefits are of less monetary significance in terms of basic retirement income adequacy for those former workers who managed to accumulate other rights or assets during their working years to serve as a source of income during retirement. While the retirement system embraced by Congress actually inspires the accumulation of such other rights and assets (purportedly for retirement uses), the creditor-protected status of those assets is much more complicated in both its technical detail and theoretical justification. As explored below, it is this more wealth-enabled group of persons and their accumulated rights and assets that the Federal Retirement Model affects most directly. With the foregoing discussion of Social Security and its anti-poverty function as a backdrop, the mechanisms of retirement policy—including the asset protection component thereof—begin to take on a somewhat different flavor.

B. Something More: Private Pensions and Personal Savings

Commentators have long recognized that Social Security alone is not sufficient to achieve the broadly stated objectives of federal retirement policy, particularly when considered in light of the lifestyle maintenance facet of those objectives.⁸⁴ Commentators have therefore recognized that a supplemental source of retirement income is both desirable and necessary.⁸⁵ The need for

83. See *supra* note 71 regarding the misconception that Social Security is a trust fund.

84. See MUNNELL, *supra* note 28, at 13 (noting how inadequacies in Social Security led to the push for private pensions); COMING OF AGE, *supra* note 58, at 11–13 (discussing the growth and design of Social Security and stating that “[w]hile Social Security alone is not sufficient at any income level to maintain preretirement living standards . . . benefits do provide a basic foundation of income support”); SASS, *supra* note 62, at 140 (noting in evaluating the early success of Social Security: “But to union members approaching retirement, Social Security benefits that replaced just one-third of their pre-retirement incomes were hardly satisfactory.”); Altman, *supra* note 58, at 494 (“[F]rom its inception, Social Security has generally been recognized as inadequate by itself to maintain the standard of living of all but the very poorest recipients.”).

85. See, e.g., 21ST CENTURY, *supra* note 57, at 17 (“[R]etirement security requires that

that supplement is more pronounced in the case of former high wage earners.⁸⁶ The reason—as suggested by the limited Social Security benefits paid under the system's progressive benefits formula—is that the higher a worker's average preretirement earnings, the more substantial the decline in the worker's standard of living upon retirement if the worker was dependent solely upon Social Security as the source of her retirement income.⁸⁷ Private pension plans and personal savings affect that supplement in varying degrees, operating as the last two "legs" of the triumvirate of federal retirement income security programs.⁸⁸

Private retirement plans come in a variety of forms.⁸⁹ Many are employer-sponsored, while others are individually directed and tend to resemble private savings arrangements as opposed to purely retirement-oriented devices. The "pension plan" designation, however, generally refers to a voluntary and employer-sponsored plan of deferred employee compensation.⁹⁰ The

public pensions be supplemented by individual savings and private pension benefits."). With respect to this concern in the crafting and adoption of ERISA, see, for example, the discussion of congressional intent and legislator comments set forth in Wohl, *supra* note 35, at 28–29 ("Congress also sought through ERISA to provide benefits to a wider group of citizens and to assist retirees in maintaining at least a minimal standard of living by securing greater benefits for retirees than would be available under Social Security." (footnotes omitted)).

86. See *supra* notes 78–79 and accompanying text (discussing the progressive and redistributive nature of the Social Security benefits structure).

87. This statement is somewhat of an overgeneralization because the worker's preretirement standard of living, relative to that in retirement, is likely to be gauged by reference to the standard of living enjoyed in the working years closest to retirement, as opposed to some average of that enjoyed over the person's working life. See MUNNELL, *supra* note 28, at 25 (noting the larger role for private pensions in providing a Social Security supplement to higher lifetime wage earners, particularly as gauged by earnings at retirement); 21ST CENTURY, *supra* note 57, at 17 ("The average monthly Social Security benefit for a retired worker in July 1998 was \$767, less than the gross monthly salary from a minimum wage job." (footnote omitted)); SASS, *supra* note 62, at 140 (discussing inadequacies of Social Security benefits to unionized laborers); see also *supra* note 67 regarding the relative distribution of Social Security benefits.

88. See, e.g., MUNNELL, *supra* note 28, at 13 (discussing the early recognition of Social Security as inadequate and the role of private pensions in addressing that inadequacy from 1935 forward); SASS, *supra* note 62, at 139–41 (discussing organized labor's role in private pension movement during the 1940s–1970s as driven in part by recognition of inadequacies of Social Security); *supra* note 85 (discussing the need for a supplemental source of retirement income).

89. See *supra* note 16 regarding the use of the generic term "retirement plan" in this Article.

90. See JOHN H. LANGBEIN & BRUCE A. WOLK, PENSION AND EMPLOYEE BENEFIT LAW 25 (3d ed. 2000) (characterizing private pension plans as voluntary, employer-sponsored, and tax-favored). More technically, ERISA distinguishes between "employee welfare benefit plans," which generally include employer sponsored plans that provide medical, vacation and similar nonretirement oriented benefits, and "employee pension benefit plans" (a/k/a "pension plans"), which generally include employer-sponsored plans that provide retirement income to employees or otherwise provide for deferral of employee income until after termination of employment.

employer's sponsorship typically consists of the employer establishing and maintaining the plan for the benefit of its employees. From the employees' perspective, "[t]he pension fund serves during the years of employment as a means of conducting a savings program for retirement . . . shift[ing] income from years of employment to years of retirement."⁹¹ Most often such plans enjoy certain tax advantages granted by the federal government in order to encourage employee participation and employer sponsorship. Tax incentives therefore play a pivotal role in the implementation of federal retirement policy.⁹² Related provisions of federal law designed to enhance the security of the retirement promise—as that promise is supported by the funds set aside in the various plan types—also play a pivotal role in this implementation. This Article discusses these matters next. It first gives brief attention to private pension plan types, and it then gives more detailed consideration to the issues of security and incentives.

1. Private Pension Plan Types

There are two broad categories of tax-favored pension plans that an employer might sponsor: defined benefit plans and defined contribution plans.⁹³ With a defined benefit (DB) plan, the employer promises to provide a certain level of benefits at retirement.⁹⁴ The employer backs that promise by contributing funds to a trust based upon actuarial assumptions about the level of funds needed to finance the promised future benefit.⁹⁵ The employer does not

ERISA, Pub. L. No. 93-406, § 3, 88 Stat. 829 (codified as amended in 29 U.S.C. §§ 1002(1)–(2)(A) (2000)). The general definition of a pension plan under the ERISA labor title, however, is not limited to those plans of deferred compensation which are tax-favored. With respect to tax incentives and plans of deferred compensation that are not eligible for such tax advantages, see *infra* note 130.

91. LANGBEIN & WOLK, *supra* note 90, at 4.

92. See *infra* Part III.C regarding the tax incentives.

93. See JCX-16-99, *supra* note 57, at 5 (describing the allocation of benefits under defined benefit and defined contribution plans); U.S. GEN. ACCOUNTING OFFICE, HEHS-00-207, CASH BALANCE PLANS 7-9 (2000) [hereinafter GAO-CASH BALANCE PLANS] (discussing defined benefit plans and defined contribution plans as types of tax-qualified pension plans), available at <http://www.gao.gov/archive/2000/he00207.pdf>; Jack VanDerhei & Craig Copeland, *The Changing Face of Private Retirement Plans, in THE FUTURE OF SOCIAL INSURANCE: INCREMENTAL ACTION OF FUNDAMENTAL REFORM?* 121, 122-23 (Edelman et al. eds., 2002) (discussing the differences between defined benefit and defined contribution plans).

94. The benefit typically is determined by reference to the employee's average pay in the last few years of work. The benefit instead might be tied to some other salary average, such as during the three years of most highly compensated employment.

95. See VanDerhei & Copeland, *supra* note 93, at 122 ("Employers offering DB plans

maintain a specific account for any individual participant. Instead, the trust is in essence a "general fund" out of which the plan pays each employee's promised benefit as the pension promise comes due.⁹⁶ The employer thus bears the risk that the contributed funds and investment returns thereon may be insufficient to fund the promised benefit, in which event the employer would have to make unanticipated additional contributions to make up any shortfall.⁹⁷

In contrast, a central aspect of a defined contribution (DC) plan is the allocation of a portion of the employee's compensation to a separate account maintained on behalf of that individual employee.⁹⁸ The benefit paid at the employee's retirement depends upon the investment performance of the separate account rather than upon some promise of a specified level of benefit. The employee bears the risk (or reaps the reward) if the investment performance of the account deviates from expectations.⁹⁹ Thus, the prospect of significant assets accumulating in a fund earmarked solely for a specific employee is inherent in the DC plan model.¹⁰⁰

must make contributions based on federal funding rules . . . in order to maintain the plan's qualified (tax-favored) status."). With regard to the use of a trust, see *infra* notes 112–14.

96. VanDerhei & Copeland, *supra* note 93, at 122 (describing defined benefit plans and defined contribution plans as types of tax-qualified pension plans).

97. See Regina T. Jefferson, *Rethinking the Risk of Defined Contribution Plans*, 4 FLA. TAX REV. 607, 610–11 (2000) (discussing how the sponsoring employer in a defined benefit plan is liable for the payment of benefits and therefore bears the risk of having insufficient assets to cover the promised payment at retirement).

98. The contribution may be made by the employee, the employer, or both. See JCX-16-99, *supra* note 57, at 5 (stating that under a defined contribution plan "an employee may elect to have the employer make payments as contributions to a qualified plan on behalf of the employee, or the employee directly in cash"); GAO-CASH BALANCE PLANS, *supra* note 93, at 8 (stating that a defined contribution plan is expressed as an individual account balance to which either the employer, the worker, or both employer and worker contribute); VanDerhei & Copeland, *supra* note 93, at 122–23 (describing defined contribution plan contributions made by both employers and employees as being placed in individual accounts). Perhaps the most well-known and prevalent type of DC plan is the tax code denominated "§ 401(k) plan," which provides generally that a specified percentage of an employee's pay can be set aside in a separate account for that employee, with the contribution coming from either or both of the employee or employer. The plan name comes from the I.R.C. provisions that authorize certain favorable tax consequences for this type of plan. See I.R.C. § 401(k) (2000) (providing the tax consequences for a cash or deferred arrangement qualified pension plan).

99. See GAO-CASH BALANCE PLANS, *supra* note 93, at 8 ("Retirement benefits are not guaranteed, and employees bear the risk of poor investment performance."); Jefferson, *supra* note 97, at 611–12 (discussing how the individual participant in a defined contribution plan bears the risk of having insufficient assets for retirement because the benefit is determined by account balance and not by a fixed amount). Plans permitted for self-employed individuals, known as Keogh or HR-10 plans, generally fall into this category of DC plans. See LANGBEIN & WOLK, *supra* note 90, at 54 (describing the origins of Keogh plans for the self-employed).

100. This prospect foreshadows the wealth accumulation dimension of the retirement plan

2. Concern for Workers' Retirement Security

A definite trend exists in the area of employer-sponsored pension plans. That trend reflects movement away from DB plans and towards DC plans, and in particular towards cash or deferred arrangements (CODAs), such as the § 401(k) plan.¹⁰¹ In reference to such trends, one might emphasize the congressional authorization of the § 401(k) plan as important in the wealth accumulation/asset protection dynamic, but that focus would be too narrow.¹⁰² The broader and more significant view reveals that congressional concern for the security of workers' retirement savings prompted the 1974 adoption of pervasive new pension legislation, popularly known as ERISA, which today serves as the foundation of the private pension system.¹⁰³ Several highly publicized scandals involving lapses in the vesting of pension plan benefits and inadequate management and funding of the plans motivated Congress to enact this "intricate and comprehensive statute" that expressly codifies as among its overriding purposes the protection of pension plan participants and their beneficiaries.¹⁰⁴ Congress granted this protection through the imposition of

asset protection dilemma, as discussed *infra* Part V.C. This possibility also harks back to the wealth accumulation and self-settlement objections attendant the more traditional spendthrift trust policy debate touched upon in *supra* Part II.

101. Profit sharing plans, stock bonus plans and other plans which include cash now/deferred compensation options are sometimes also referred to as a qualified cash or deferred arrangements (CODAs). See generally JCS-3-95, *supra* note 63, at 15 (discussing special rules that apply to qualified cash or deferred arrangements). As to the trend, see generally Jefferson, *supra* note 97, at 614-15, listing reasons for this shift as: (1) less onerous administrative burdens and costs for DC plans; (2) more frequent changes in the laws relating to DB plans; and (3) employee preference for flexibility, vesting schedules, and participant involvement in DC plans.

102. See Revenue Act of 1978, Pub. L. No. 95-600, §135, 92 Stat. 2763, 2785-2787 (codified at I.R.C. § 401(k)) (amending I.R.C. § 401 and authorizing new § 401(k)).

103. ERISA, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 26 U.S.C. and 29 U.S.C.); see JCX-16-99, *supra* note 57, at 2 ("The present-law rules governing qualified plans originated in the Employee Retirement Income Security Act of 1974 . . . [which] forms the basis for the current private pension system."). "Retirement income security" generally refers to the broad objective of insuring adequate retirement income, and should not refer to the more narrow idea of protecting retirement assets from creditor claims. See *supra* Part III.A (discussing Social Security benefits as providing a floor for insuring adequate retirement income).

104. See ERISA § 2 (declaring the policy of the statute to include protecting the interests of participants in employee benefit plans and their beneficiaries); 29 U.S.C. § 1001 (2000) (same); *Boggs v. Boggs*, 520 U.S. 833, 841 (1997) (discussing ERISA as an "intricate, comprehensive statute" whose provisions provide detailed protections to the spouses of plan participants); see also LANGBEIN & WOLK, *supra* note 90, at 68-84 (discussing the Studebaker incident and the legislative history of ERISA); SASS, *supra* note 62, at 191-202 (discussing incidents preceding the enactment of ERISA); William J. Chadwick & David S. Foster, *Federal Regulation of*

minimum requirements for reporting, disclosure, participation, vesting, funding, and fiduciary conduct with respect to covered plans.¹⁰⁵ These requirements are set forth in dual and often overlapping labor and tax provisions.¹⁰⁶

3. *The ERISA Labor Mandate*

Although ERISA is directed most specifically at assuring that employee benefit plans are financially sound and fair in their treatment of employees,¹⁰⁷ ERISA also requires that covered pension plan benefits be facially sheltered from employees' creditor claims by the umbrella of an anti-alienation provision.¹⁰⁸ As set forth in the statutes, this anti-alienation provision "looks strikingly like language describing a traditional spendthrift trust."¹⁰⁹ Specifically, in ERISA § 206(d)(1), Congress mandated that "[e]ach pension plan shall provide that benefits . . . under the plan may not be assigned or

Retirement Plans: The Quest for Parity, 28 VAND. L. REV. 643, 668–81 (1975) (tracing the origins and operation of ERISA).

105. See ERISA § 2 (declaring that ERISA interests will be protected by requiring disclosure, establishing standards of conduct, and providing for remedies); 29 U.S.C. § 1001(b) (same).

106. Codification in Titles 26 and 29 of the U.S. Code reflects the dual nature of ERISA as both a labor and a tax statute, with the tax provisions now appearing with the rest of the Internal Revenue Code in Title 26 and the Treasury Department regulations thereunder. Regulations promulgated by the Department of Labor accompany the labor provisions in Title 29. The labor provisions identify various types of plans and the standards to which they are subject, while the tax provisions specify attributes required in order for a plan to qualify for the favorable tax treatment that is so fundamental to many such plans. See 29 U.S.C. §§ 1001–1461 (providing the ERISA labor provisions); I.R.C. §§ 401–420 (2000) (providing a sampling of ERISA tax provisions); see also *In re Sewell*, 180 F.3d 707, 710 (5th Cir. 1999) ("ERISA is a largely parallel, dual system, jointly administered by the Department of Labor and the Department of the Treasury, and statutorily bifurcated into Titles 26 and 29 of the U.S. Code."); JCX-16-99, *supra* note 57, at 25 (discussing the dual aspects of ERISA). A review of the various reporting, disclosure, participation, vesting, funding, and fiduciary requirements of ERISA is beyond the scope of this Article.

107. See ERISA § 2 (finding it desirable to assure "the equitable character of such plans and their financial soundness"); 29 U.S.C. § 1001(a) (same).

108. The anti-alienation provision set forth in the ERISA labor title is found in ERISA § 206(d)(1), 29 U.S.C. § 1056(d)(1), and is hereinafter referred to in the text as "ERISA § 206(d)(1)." The comparable tax provision is found in I.R.C. § 401(a)(13), as discussed *infra* in the text accompanying notes 123–26.

109. Wohl, *supra* note 35, at 16; see also *Sewell*, 180 F.3d at 709 ("Among other typical ERISA provisions, the Plan contains . . . an anti-alienation or 'spendthrift' clause . . ."). *Supra* notes 18–21 discuss spendthrift trusts and the anti-alienation provisions that underlie their protective nature.

alienated."¹¹⁰ The technical definition of "pension plans" is broad,¹¹¹ and thus the anti-alienation mandate applies to the bulk of private employer-sponsored retirement arrangements established to benefit employees. In most instances, the provision of benefits must be accomplished via utilization of a trust that holds the assets from which such benefits ultimately are paid.¹¹² The association between employer-sponsored pension plans and traditional spendthrift trusts therefore was an easy one to make in the formative stages of the Federal Retirement Model's asset protection dynamic.

Exceptions exist, however, to the ERISA labor title's coverage, its trust requirement, and its anti-alienation mandate.¹¹³ Individual Retirement Arrangements (IRAs)—which are more like tax-favored individual savings accounts than pension plans—are important among the arrangements excepted from ERISA § 206(d)(1).¹¹⁴ ERISA also excepts plans established by the self-

110. ERISA § 206(d)(1); 29 U.S.C. § 1056(d)(1). It also should be noted that a handful of specific but limited types of assignments are still permitted, even when ERISA § 206(d)(1) does apply. Specifically permitted are: (1) voluntary and revocable assignments of not more than 10% of any benefit payment; (2) assignments relating to qualified domestic relations orders as described in I.R.C. § 414(p) or 29 U.S.C. § 1056(d)(3)(B); and (3) certain assignments made as security for a limited class of loans made from the plan to a participant or beneficiary. See ERISA §§ 206(d)(2)–(3) (setting forth the permitted assignments); 29 U.S.C. §§ 1056(d)(2)–(3) (same); I.R.C. §§ 401(a)(13)(A)–(B) (providing that a trust will not be qualified if it is assignable but also setting forth permitted assignments).

111. As discussed *supra* note 90, for purposes of the labor title, "pension plan" as defined under ERISA encompasses private employer-sponsored plans that provide retirement income to employees or otherwise provide for deferral of employee income until after termination of employment. See ERISA § 3(2)(A) (defining "employee pension benefit plan" and "pension plan"); 29 U.S.C. § 1002(2)(A) (same); ERISA § 3(3) (providing that "employee benefit plan" includes "pension plan"); 29 U.S.C. § 1002(3) (same); ERISA § 4(a) (delineating ERISA coverage); 29 U.S.C. § 1003(a) (same); see also *infra* note 123 (discussing the term "qualified trust").

112. See ERISA § 403(a) (providing that all assets of an employee benefit plan shall be held in a trust); 29 U.S.C. § 1103(a) (same).

113. The most important exceptions to the trust requirement relate to assets held under certain types of insurance contracts, individual retirement accounts that are custodial in nature, and I.R.C. § 403(b) annuity contracts. See ERISA § 403(b) (providing exceptions to the requirement that all assets of an employee benefit plan shall be held in a trust); 29 U.S.C. § 1103(b) (same); see also *infra* note 128 (regarding trust status under the tax provisions of ERISA). Some courts, however, have read the Supreme Court's pronouncements in this area, as discussed *infra* Part IV.B.2, as expanding the scope of ERISA's protection to retirement vehicles that are not in trust form. See, e.g., *In re Barnes*, 264 B.R. 415, 421–29 (Bankr. E.D. Mich. 2001) (discussing cases that support the notion that any plan subject to ERISA § 206(d)(1) can be excluded from the bankruptcy estate under 11 U.S.C. § 541(c)(2) without regard to whether or not the plan is in the form of a trust).

114. The IRA is a type of tax-favored personal savings plan originating in 1974 under ERISA as a tax-favored retirement savings opportunity to those individuals not participating in an employer-sponsored plan. See ERISA § 2002 (amending the Internal Revenue Code to

employed (Keogh plans) where partners or sole owners, but generally not employees, are the only participants.¹¹⁵ ERISA also excepts other unfunded or employer-specific plans such as those for governmental, church, and charitable employees.¹¹⁶ The ERISA § 206(d)(1) mandate therefore is quite pervasive, but leaves many arrangements to other protective considerations.¹¹⁷ Fully grasping the nature and import of this complex asset protection scheme requires an understanding of the ERISA labor title's anti-alienation mandate in context with a corresponding mandate set forth in the ERISA tax title, as is discussed next.¹¹⁸

C. Tax Qualification and the Incentive Trade-off

In contrast to the mandatory Social Security program, employer sponsorship of a pension plan is voluntary, as is an individual's decision to save.¹¹⁹ The federal government does, however, provide certain incentives designed to encourage these activities. Internal Revenue Code provisions reflect the primary incentives. Those provisions grant favorable tax treatment

include IRAs). Part 2 of Title I of ERISA—which includes the § 206(d)(1) spendthrift mandate of the labor title—excepts these arrangements by operation of ERISA § 201(6), 29 U.S.C. § 1051(6).

115. See 29 C.F.R. §§ 2510.3-3(b)–(c) (2002) (excepting plans without employees); see also *infra* notes 135–140 and accompanying text (regarding Keogh plans).

116. See ERISA § 403(b) (excluding from scope of § 206(d)(1) the enumerated types of plans); 29 U.S.C. § 1103(b) (same). ERISA § 403(b) also excepts certain insurance policies or contracts and for amounts held in qualifying custodial accounts. ERISA's entire labor provisions exclude annuity plans of certain charitable employers such as educational institutions, as well as "excess benefit" plans established to permit contributions and to provide benefits in excess of tax code limitations. See ERISA § 4(b) (providing broader exceptions to coverage under any of the ERISA labor title); 29 U.S.C. § 1003(b) (same). As seen *infra* Part IV, these distinctions are directly relevant to defining the paths to asset protection under the Federal Retirement Model.

117. Such considerations are discussed more fully *infra* Part IV.B.3.

118. See *supra* note 9 regarding the codification of ERISA in Title 29 (labor provisions) and Title 26 (tax provisions) of the U.S. Code.

119. See GAO-CASH BALANCE PLANS, *supra* note 93, at 11 ("Federal law does not require that employers sponsor pension plans nor does it mandate the value of the benefit provided by plans that the employer voluntarily sponsors."); COMING OF AGE, *supra* note 58, at 11–13 (discussing the voluntary nature of the pension system and the influences upon worker participation); Peter M. van Zante, *Mandated Vesting: Suppression of Voluntary Retirement Benefits*, 75 NOTRE DAME L. REV. 125, 128–41 (1995) (same); Paul J. Yakoboski, *Retirement Plan Design and Policy into the 21st Century*, 56 N.Y.U. INST. ON FED. TAX'N 2-1, 2-5–2-6 (Supp. 1998) (detailing statistics on voluntary participation in pension plans since enactment of ERISA).

where funds are set aside in a "tax-qualified" pension or retirement savings plan that conforms to certain requirements and limitations.¹²⁰ Accepting these requirements and limitations is in effect a trade-off for workers—and in the case of employer-sponsored pension plans, for the sponsoring employer—of receiving the favorable tax treatment.

1. *The Immediate Trade-off: Conditioned Tax Incentives*

Commentators therefore describe Congress's approach to the private pension and retirement savings plan area as grounded in a "carrot and stick" mentality. The "carrot" represents the tax incentives, and the "stick" represents the requirements and limitations that adhere to the favorably treated plan in order to ostensibly further the underlying goals of retirement income security.¹²¹ For most plans, a prerequisite to receiving such favorable tax treatment is that plan contributions be made to a trust meeting certain delineated requirements.¹²² Of particular interest in this regard is the anti-alienation requirement embodied in the ERISA tax title at I.R.C. § 401(a)(13). That provision specifies that a retirement "trust shall not constitute a qualified trust [eligible for favorable tax treatment] . . . unless the plan of which such trust is a

120. The author uses "tax-qualified" here to describe generally a retirement plan that conforms to the tax code prerequisites for receiving the favorable tax treatment described in Part III.C. Specifics may be found in I.R.C. §§ 401–420 (2000). See ERISA § 2 (noting revenue loss to government attributable to preferential tax treatment accorded certain retirement plans), 29 U.S.C. § 1001 (same); JCX-16-99, *supra* note 57, at 4 (discussing the use of tax policy to motivate pension funding as a source of retirement income); COMING OF AGE, *supra* note 58, at 11 (same). With regard to the distinction between "tax-qualified" and "ERISA-qualified," see *infra* notes 223–227 and accompanying text.

121. See, e.g., Daniel I. Halperin, *Special Tax Treatment for Employer-Based Retirement Programs: Is It "Still" Viable as a Means of Increasing Retirement Income? Should it Continue?*, 49 TAX L. REV. 1, 6–7 (1993) (stating that "[a]t the same time as the stick (restrictions) has become heavier, the carrot (tax relief) has become less sweet"); IPPOLITO, *supra* note 82, at 174 (noting favorable tax treatment coupled with conformity to certain rules necessary to receive this treatment: "Two aspects of the tax code dominate the treatment of savings for retirement"); see also GAO-CASH BALANCE PLANS, *supra* note 93, at 6 ("Congress has used the [Tax] Code to encourage employers to sponsor pensions to help workers achieve adequate income for retirement. In exchange for providing preferential tax treatment, Congress has imposed requirements that plans must meet for tax qualification . . ."); Dilley, *supra* note 66, at 1141 ("In effect, the Code uses a carrot-and-stick approach to encourage employers to set up pension plans for their work forces—the carrot is the tax benefit of establishing a qualified pension plan and the stick is the limit on that benefit . . ."); van Zante, *supra* note 119, at 134 ("[T]he price of qualification for this income tax treatment is conformity to a system of minute regulation . . .").

122. See I.R.C. § 401(a) (setting forth the requirements for qualified trusts).

part provides that benefits provided under the plan may not be assigned or alienated."¹²³ In contrast to the anti-alienation language that *must* be included in a plan that is subject to § 206(d)(1) of the ERISA labor title, however, no trust is *required* to include the anti-alienation language described in the tax title at I.R.C. § 401(a)(13).¹²⁴ Moreover, no enforcement mechanism exists if the I.R.C. § 401(a)(13) restraint is violated or simply omitted.¹²⁵ Instead, the I.R.C. § 401(a)(13) anti-alienation provision is a price to be voluntarily paid (i.e., the "stick") only by those who desire favorable tax treatment (i.e., the "carrot").¹²⁶ Some arrangements, however—most notably IRAs and non-employee Keogh plans—may qualify for favorable tax treatment notwithstanding the absence of an I.R.C. § 401(a)(13) anti-alienation provision.¹²⁷ Limited exceptions exist as to the trust requirement as well.¹²⁸

123. I.R.C. § 401(a)(13); *see also* Treas. Reg. § 1.401(a)-13 (1988) ("Under section 401(a)(13), a trust will not be qualified unless the plan of which the trust is a part provides that benefits provided under the plan may not be . . . assigned . . . alienated . . ."). While the trust technically qualifies by virtue of the spendthrift restraint and the plan then qualifies by virtue of the utilization of a qualified trust, the terms "tax-qualified plan" and "tax-qualified trust" are used interchangeably here, consistent with common parlance identifying a plan which conforms to the tax code prerequisites for receiving such favorable tax treatment as a "qualified plan." *See supra* note 120 (defining tax qualified). For similar short-hand phraseology, *see, for example*, BORIS L. BITTKER & LAWRENCE LOKKEN, *FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS* § 61.2 (2d ed. vol. 2, 1990).

124. *See* I.R.C. § 401(a)(13) (providing that a trust will not be a qualified trust unless it meets the requirements for an anti-alienation provision); Treas. Reg. § 1.401(a)-13 (1988) (providing that a trust must provide that benefits may not be alienated in order to be qualified).

125. *But see infra* note 232 and accompanying text (discussing how the I.R.C. § 401(a)(13) anti-alienation provision still may be given effect).

126. Although the legislative history is devoid of content on the point, it seems clear that at the time enacted, Congress envisioned the anti-alienation provision requirements correspondingly set forth in the ERISA tax and labor titles to be a "stick" of general (though not universal) applicability. *See* Dilley, *supra* note 35, at 396-98 (stating that Congress included the anti-alienation provisions of ERISA as part of the vesting requirements which represent a clear constraint on employer behavior). The delineation of the I.R.C. anti-alienation provisions within the context of qualified trust requirements supports this characterization as a "stick" in the overall incentive scheme. Further supporting this view is the association of the ERISA spendthrift mandate with the vesting rules attendant covered plans, and in particular, as a reinforcement of the limitation on employee access to plan funds under the dominant DB plan type at the time of ERISA's enactment. For analysis that supports this view, *see* Dilley, *supra* note 35, at 396-99.

127. For additional insight into this treatment of IRAs and Keogh plans, *see* the text accompanying *infra* notes 135-41.

128. Like the ERISA labor provisions, the tax code provisions focus on the trust as the pervasive vehicle for retirement plan asset management. *See, e.g.*, I.R.C. § 402(a) (providing tax deferral for contributions to qualified trusts); *id.* § 401(a) (setting forth requirements for qualified trusts). However, as under the labor title, the provisions make exceptions for certain insurance policies or contracts and for amounts held in qualifying custodial accounts. *See supra*

As to the "carrot," the tax incentives operate on three fronts. First, workers receive a significant and immediate tax incentive via the ability to exclude from gross income the amounts set aside in a tax-qualified retirement plan.¹²⁹ Simply stated, the employee can defer tax liability upon the amounts set aside until those amounts actually are distributed to the employee, which often is decades in the future.¹³⁰ The second key tax incentive pertains to the

note 113 (discussing exceptions under the labor title); *see, e.g.*, I.R.C. § 404(a)(1)–(5) (setting forth tax deduction provisions for contributions to qualified trusts, annuity plans, and other arrangements). Despite the absence of a formal trust, however, the statute may accord such arrangements treatment comparable to that of a qualified trust, including treatment indicating the inclusion of the anti-alienation provision called for under I.R.C. § 401(a)(13). *See, e.g.*, I.R.C. § 401(f) (stating that custodial accounts, annuities, and other contracts issued by an insurance company "shall be treated as a qualified trust" if the requirements pertaining to such trusts are otherwise met); *id.* § 404(a)(2) (establishing compliance with I.R.C. § 401(a)(13) anti-alienation provision as requirement for tax-qualified employee annuities); *see also* BITTKER & LOKKEN, *supra* note 123, §§ 61.2, 61.15 (discussing qualified trust and qualified plan requirements); MICHAEL J. CANAN, QUALIFIED RETIREMENT PLANS § 7.3 (2003 ed. vol. 1, 2002) ("However, the custodian [of an account created in lieu of a trust] will be treated as trustee [A] qualified annuity plan does not need to have a trust However, a common practice with a plan in which individual annuity policies are issued is to have a trust agreement" (footnotes omitted)); LANGBEIN & WOLK, *supra* note 90, at 222 ("Annuity plans . . . do not have a trust [but nevertheless] must meet essentially all of the requirements of I.R.C. § 401(a) Accordingly, we shall ignore any distinction . . ."). The author will pursue further exploration of these finer distinctions and non-trust vehicles in the specific context of the applicable asset protection legal framework described *infra* Part IV. The Federal Retirement Model is grounded in the spendthrift trust type arrangement, but is more appropriately conceived as encompassing related vehicles ostensibly authorized and encouraged to promote retirement income security objectives. *See In re Barnes*, 264 B.R. 415, 421–29 (Bankr. E.D. Mich 2001) (discussing cases that support the notion that any plan subject to ERISA § 206(d)(1) can be excluded from the bankruptcy estate under 11 U.S.C. § 541(c)(2) without regard to whether or not the plan is in the form of a trust).

129. This is the case even though the tax-qualified plan may be funded and the employee's rights are therein vested. *See* I.R.C. § 402(a) (providing for the taxation of the amount distributed under an exempt employees' trust in the taxable year in which it is distributed). *See generally* JCX-16-99, *supra* note 57, at 5–8 (discussing operative tax treatment of tax qualified plans and similar arrangements).

130. Otherwise applicable U.S. income tax rules generally dictate that earnings from employment are included in gross income and therefore taxed to the employee in the year received by or set aside for the benefit of the employee. The employee's liability for taxes due on such earnings therefore would serve to reduce the net amount of earnings ultimately retained by the employee for investment to support retirement. The exclusion from gross income provided under the retirement plan tax incentive, in contrast, abrogates such tax liability with respect to contributions to the plan whether the contributions are made by the employee or by the employer on behalf of the employee. *See* I.R.C. § 61(a)(1) (providing that gross income includes compensation for services rendered); *Id.* §§ 83(a), (h) (coordinating employee's inclusion of property received in exchange for services with employer's deduction); *Id.* § 402(b) (providing that employee is currently taxable on contributions made to a trust that is not tax-qualified); Rev. Rul. 60-31, 1960-1 C.B. 174 (discussing tax inclusion issues of constructive receipt and economic benefit). These rules generally mean that amounts paid to or set aside for

amounts set aside. Specifically, earnings on contributions to the plan accumulate on a tax-free basis until withdrawn, thus permitting compounded growth of the fund without annual reduction for taxes due on investment earnings.¹³¹ These employee-targeted tax incentives are believed to motivate employees to pressure employers for the payment of some portion of wages through a tax-qualified deferred compensation arrangement.¹³²

The third tax-incentive focuses more directly upon employers. Specifically, for an employer contributing funds to a tax-qualified plan on behalf of an employee, an incentive is provided in the form of an immediate tax deduction for the contribution as compensation paid, even though the amount contributed will not be included in the employee's gross income until

an employee under a nontax-qualified *deferred* compensation arrangement (a "nonqualified deferred compensation" (NQDC) arrangement) will be taxable to the employee in the year the services are performed, despite the absence of immediate cash compensation, unless the plan is unfunded or the employee's interest is subject to a substantial risk of forfeiture. *See generally* CANAN, *supra* note 128, § 2.3 (discussing taxation of employee compensation generally, and in particular NQDC arrangements); LANGBEIN & WOLK, *supra* note 90, at 249–70 (discussing taxation of NQDC arrangements); Chadwick & Foster, *supra* note 104, at 690–91 (discussing taxation of NQDC arrangements after ERISA); Norman P. Stein, *Qualified Plans and Tax Expenditures: A Reply to Professor Zelinsky*, 9 AM. J. TAX POL'Y 225, 226–27 (1991) (discussing taxation of unfunded deferred compensation arrangements). Note that, in some situations, an employee may be taxed at the time of an employer contribution to a NQDC plan, and then can be taxed again when distributions relating to that contribution are received from the plan. CANAN, *supra* note 128, § 2.3 (discussing the collective operation of I.R.C. §§ 72, 83(a), & 402(b)).

131. *See* I.R.C. § 401(a) (setting forth the requirements for qualified trusts); *id.* § 402(a) (providing tax deferral for qualified trusts); *id.* § 408(e) (exempting individual retirement accounts); *id.* § 501(a) (exempting qualified trusts). It is possible to set up an unfunded plan of NQDC, which results in neither a current outlay by, nor deduction to, the employer, as well as no current gross income to the employee. Such an arrangement, however, lacks the attribute of tax-free earnings accumulation, and therefore the value of the future benefit will presumptively be less. Outside the tax-qualified arena, interest or similar earnings on investments generally are subject to, and thus reduced by, taxes each year, again serving to reduce the amount that would ultimately be available for retirement needs. *See, e.g.*, I.R.C. §§ 61(a)(4)–(7) (stating that gross income includes interest, rents, royalties and dividends). Of course, the funds could be invested in assets which produce tax-exempt earnings, but the promised investment return on such assets is generally acknowledged to be lower by virtue of their tax-free nature. To the extent the employee's preferences and circumstances leave room for other than current consumption of earnings, the unique tax treatment of both the deferred wage and savings elements of the tax-qualified arrangement provide a definite incentive relative to the otherwise available compensation and savings options. As to current consumption needs and the ability to take advantage of the tax incentive, *see infra* notes 145–148.

132. The significance of this belief is discussed in the text accompanying *infra* notes 155–158, and again from a more evaluative point of view in Part V.B.1.

withdrawn from the tax-qualified plan.¹³³ The special tax treatment therefore lowers the relative cost to the employer of paying *deferred* compensation.¹³⁴

Tax incentives of similar import exist outside the employer-sponsored plan context. Self-employed persons, for example, may elect to participate in Keogh plan arrangements that offer tax benefits comparable to those described above with respect to employer-sponsored plans.¹³⁵ Tax-free contributions and

133. See I.R.C. § 404(a) (providing for deduction of employer's contributions to an employees' trust or annuity plans). The employer's contribution is in the nature of compensation to the employee, since the contribution is made in recognition of services provided to the employer by the employee—in other words, the employer's contribution is the equivalent of a choice of deferred compensation in lieu of current cash compensation by the employee. See Stein, *supra* note 130, at 242–43 (noting that the special tax rules reduce costs of paying deferred compensation, essentially equating the cost of paying deferred compensation to that of paying immediate compensation by virtue of the availability of an immediate tax deduction in either case); *supra* note 130 and accompanying text (discussing tax consequences of employee compensation and NQDC arrangements). All other things being equal, the tax incentive leaves the employer indifferent as between paying *current* cash compensation or *tax-qualified deferred* compensation. In either case, an immediate deduction is available for the amount paid to or contributed on behalf of the employee. See Bruce Wolk, *Discrimination Rules for Qualified Retirement Plans: Good Intentions Confront Economic Reality*, 70 VA. L. REV. 419, 430 (1984) ("Whether as a \$1,000 wage payment or as a \$1,000 contribution to a qualified retirement plan, the employer can deduct the total amount as a business expense.") All other things are not equal, however, as employers may have nontax reasons for establishing a retirement plan of deferred compensation. See, e.g., Jonathan Barry Forman, *How Federal Pension Laws Influence Individual Work and Retirement Decisions*, 54 TAX LAW. 143, 165–70 (2000) (discussing the impact of federal laws upon retirement decisions); Halperin, *supra* note 121, at 7–9 (making similar observations); Stein, *supra* note 130, at 240–43 (discussing employer and employee preferences for deferred compensation that are motivated by non-tax considerations); van Zante, *supra* note 119, at 144 (noting employer motivation of increased employee tenure coupled with facilitation of retirement for less productive older workers).

134. Moreover, an employer contributing funds on behalf of an employee to a plan of deferred compensation that is *not* tax-qualified (a "nonqualified deferred compensation" (NQDC) plan) typically would not receive a deduction until the contributed funds are included in the employee's gross income. This generally occurs only when the employee receives the contributed funds or the economic benefits thereof. See I.R.C. §§ 404(a)(5), 404(b) (providing that outside the tax qualified plan context, the employer's deduction is delayed until the amount contributed is included in the employee's gross income). With respect to NQDC plans and the time at which such amounts might be included in the employee's gross income and therefore subject to tax, see *infra* note 130 and accompanying text.

135. Regarding Keogh plans, also see the text accompanying *supra* note 115. A statutory artifice that renders such persons both employer and employee for purposes of receiving the tax-favored deferral/deduction treatment noted above confers the noted benefits. See I.R.C. §§ 401(c)(1), 401(c)(4) (treating self-employed individuals, sole owners, and members of a partnership as employees); LANGBEIN & WOLK, *supra* note 90, at 223 (noting that these I.R.C. provisions treat such individuals as employees for qualified plan purposes, while simultaneously deeming such individuals an employer for contribution purposes—"The net result is that contributions to the plan are currently deductible and income is deferred until distribution").

earnings also are an essential characteristic of the IRA.¹³⁶ The exact placement of Keogh plans and IRAs in supporting the three-legged stool of retirement income security is debatable, however, despite similarities to the tax incentive approach applicable to employer-sponsored plans. On the one hand, Keogh plans and IRAs are not typically employer-sponsored, often have no employees apart from the owner/settlor, and most often are subject to unilateral participant control.¹³⁷ These arrangements therefore appear to be nothing more than a tax-

136. See I.R.C. §§ 219, 408(a) (defining and setting the qualifications for an IRA and allowing a deduction for retirement savings). Here, the key incentive to a contributing individual is in the nature of a deduction for gross income which ultimately serves to reduce the amount of income subject to taxation on a dollar-for-dollar basis. This essentially means that before-tax dollars can be set aside in a tax-free investment vehicle, just as in the case of an employer-sponsored plan. See I.R.C. §§ 62(a)(7), 219 (providing deduction provisions relevant for contributions to IRAs); *id.* § 408(e)(1) (exempting IRAs from taxation). A key variation on this theme is the relatively recent addition of the "Roth IRA," in which after-tax dollars are set aside in an account meeting certain conditions, but thereafter the funds may grow and be withdrawn without reduction for taxes due, thus providing a similarly (but back-loaded) tax incentive-laden savings vehicle. See I.R.C. § 408A (defining and providing the qualifications for a Roth IRA). See generally Regina T. Jefferson, *A Farewell to Pension Policy: The Impact of Flexible IRAs on Current Tax Policy*, 69 TEMPLE L. REV. 1451, 1456-57 (1996) (describing the function and purpose of the Roth IRA); Richard L. Kaplan, *Retirement Funding and the Curious Evolution of Individual Retirement Accounts*, 7 ELDER L.J. 283, 287-88 (1999) (discussing tax consequences of the Roth IRA); Gary S. Lesser, *The New Roth IRA Rules: A Small Price for the Benefits*, 6 J. TAX'N EMPLOYEE BENEFITS 147 (1998) (discussing the benefits of the Roth IRA). Other variations on the IRA theme include the SIMPLE plan (which can exist in either IRA or 401(k) form) and SEPs. See JCX-16-99, *supra* note 57, at 5-6 (describing the SIMPLE and SEP retirement plans).

Excepting only a period of liberalization in the early 1980s, the rules governing IRAs have remained fairly constant since the Tax Reform Act of 1986, although recently passed legislation raises the annual limit on the amounts an individual may contribute to such an arrangement gradually from \$2,000 to \$5,000 through 2008. See Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), Pub. L. No. 107-16, § 611(d)(1), 115 Stat. 3897, 3897-98 (codified at I.R.C. § 402(g)) (increasing the maximum dollar amount an individual can defer). With respect to the history of IRA legislation and amendments thereto, see generally, JCS-3-95, *supra* note 63, at 1; LANGBEIN & WOLK, *supra* note 90, at 54-55; Chadwick & Foster, *supra* note 104, at 692-97; Kaplan, *supra*, at 284-88. EGTRRA also provides for a raising of the limits on annual contributions to other types of retirement arrangements. For example, the annual limit on the amount which may be contributed by or on behalf of an employee to a DC plan has been increased to the lesser of \$40,000 or 100% of annual compensation, and the amount of employee's elective deferral (upon which cost of living adjustments will be made) will rise from a base of \$10,500 in 2001 to \$15,000 by 2006. EGTRRA §§ 611(b), 632 (amending I.R.C. § 415(c)(1)). With respect to DB plans, the statute raises the annual limit on benefits payable in 2002 to \$160,000 (thereafter adjusted for cost-of-living increases), or 100% of the participant's average compensation over the participant's highest three compensation years. *Id.* § 611(a) (amending I.R.C. § 415(b)(1)(A)).

137. See DeVaney & Chien, *supra* note 67, at 72 (distinguishing IRAs and Keogh plans from defined contribution plans). Variations such as the SIMPLE plan, which entails employer sponsorship and may exist as either an IRA or 401(k) arrangement, and the SEP arrangement,

avored personal savings opportunity.¹³⁸ On the other hand, Keogh plans accord employer-sponsored plan equivalency to plans established by the self-employed.¹³⁹ Congress similarly conceived the IRA as a fair alternative for those not participating in employer-sponsored plans.¹⁴⁰ The IRA also is a frequent receptacle for funds "rolled-over" from a tax-qualified employer-sponsored retirement plan as a means of continuing the tax-deferral opportunity.¹⁴¹

For reasons mentioned and others that the author will make apparent, however, this Article treats non-employee Keogh plans and IRAs as distinct from more traditional employer-sponsored retirement arrangements. Among other concerns, the existence of tax-favored non-employee Keogh plans and IRAs combined with the limits on the applicability of the ERISA anti-alienation mandate produces a divided approach to asset protection within the Federal Retirement Model.¹⁴² One effect of that division is a continuing role for traditional spendthrift trust concepts and bankruptcy exemption planning ideas in resolving retirement plan asset protection issues.¹⁴³ Two other issues that the federal tax incentive approach to motivating retirement plan participation raises also are critical to evaluating asset protection within the Federal Retirement Model. Those issues are the tax expenditure cost to the federal government of

whereby an employer contributes to an IRA on behalf of an employee, complicate such generalizations. See JCX-16-99, *supra* note 57, at 5-6 (discussing employer involvement in SIMPLE and SEP retirement plans).

138. See, e.g., 21ST CENTURY, *supra* note 57, at 21 (considering IRAs as an aspect of the personal savings leg of the stool).

139. See *supra* note 135 and accompanying text (discussing a statutory artifice that treats self-employed persons as both employer and employee).

140. The IRA originated in 1974 under ERISA as a retirement savings vehicle for those individuals not participating in an employer-sponsored retirement plan. See ERISA, Pub. L. No. 93-406, § 2002, 88 Stat. 829, 959-64 (codified at I.R.C. §§ 408, 219) (amending the Internal Revenue Code to include a provision for individual retirement accounts); *supra* note 114 (discussing the origins of the IRA).

141. See I.R.C. § 402(c) (setting forth rules relating to rollovers from exempt trusts); JCX-16-99, *supra* note 57, at 19 (summarizing the rules for "eligible rollover distributions"); DeVaney & Chien, *supra* note 67, at 73 ("In addition to acting as a substitute for employer-sponsored plans, IRAs may be used as a means of rolling over a tax-deferred pension plan when a worker is changing jobs or retiring."); VanDerhei & Copeland, *supra* note 93, at 127 (noting that 37% of participants removing assets from § 401(k) plans rolled the amounts over into an IRA).

142. *Supra* Part III.B.3 discusses limits on the applicability of the ERISA anti-alienation mandate. The divided nature of the Federal Retirement Model and the circumstances that have led to that division are the topic of *infra* Part IV.B of this Article.

143. See Part IV.B.2 for an exposition of this result.

providing the noted retirement plan tax incentives and the equity issues thereby raised.

2. *The Broader Trade-off: Equity and the Tax Expenditure*

Despite the noted tax-based incentives for participating, not all workers choose to fund a private retirement plan.¹⁴⁴ Many workers do not participate because they lack any discretionary income above the amount required to meet current basic needs. In other words, they currently lack the resources to set aside funds today for future consumption. These and other realities lead to frequent criticism of the tax-incentive approach to promoting retirement income security outside the Social Security context, because the incentives, which come at significant cost to federal revenues, are meaningless to those unable to take advantage of them due to a lack of resources.¹⁴⁵ Moreover, the tax incentives are of different value to different workers. Specifically, high-income workers subject to taxation at relatively higher marginal rates derive the most value.¹⁴⁶ These tax payers value the incentive more because the benefit of tax deferral increases as marginal tax rates rise based upon the greater amount that would otherwise be paid in current taxes absent the favorable tax treatment.¹⁴⁷

144. Statistics in this regard are summarized in JCX-9-02, *supra* note 16, at 29–33. The report notes that in 1999, 56% of full-time private sector workers participated in employer-sponsored tax-qualified retirement plans, with 42% participating in DC plans and 25% in DB plans, with some employees participating in both. *Id.* at 29. The growth of DC plans relative to DB plans since 1978 is also shown to be significant. *Id.* at 32.

145. See Bankman, *supra* note 73, at 821 ("A large portion of the income earned by low-paid employees goes to purchase necessities and near-necessities. Forced purchase of retirement benefits might deprive such employees of funds currently needed to raise families or otherwise maintain a barely adequate lifestyle."); Graetz, *supra* note 58, at 878 (noting that additional tax incentives for deferred compensation plans are unlikely to entice those already contributing to Social Security through payroll taxes and thus having little income to spare); Halperin, *supra* note 121, at 14 ("Lower income employees cannot be expected to provide for the future when current income is barely adequate for a minimum standard of living."); Stein, *supra* note 130, at 244–48 (discussing how current consumption motivations reduce the desire to set aside funds in a deferred compensation plan); Wolk, *supra* note 133, at 430–31 (stating that current consumption needs of lower wage earners impact their ability to save).

146. See Dille, *supra* note 35, at 406 (stating that the private pension tax expenditure favors "higher income workers, male workers, and white workers").

147. See *id.* at 406–07 (detailing the benefits of deferred taxation to upper income taxpayers). For example, if Worker A is subject to a 40% marginal tax rate, but can receive \$1,000 tax-free by placing that amount in a tax-qualified plan, Worker A "saves" \$400 in taxes by doing so (i.e., $\$1,000 \times 40\% \text{ tax rate} = \$400 \text{ taxes otherwise due}$). In contrast, if Worker B is subject to a 10% marginal tax rate, placing the same \$1,000 in a tax-qualified plan only "saves" Worker B \$100 in taxes (i.e., $\$1,000 \times 10\% \text{ tax rate} = \$100 \text{ taxes otherwise due}$). Consequently, the tax incentive is "worth" \$300 more to Worker A. The example is accurate

The result of this tax-incentive approach to promoting retirement income security is that the federal "retirement income system produces two discrete classes of retirees: those who rely solely on Social Security and those who receive employer provided pensions or some other supplemental source of income."¹⁴⁸

Such considerations raise equity and fiscal concerns regarding the incentives provided for the pension and savings aspects of the retirement income security system. From the employees' perspective, a distortion in vertical equity occurs because "the higher paid participate in greater numbers, are entitled to larger benefits per person and save more in taxes for each dollar contributed."¹⁴⁹ On the federal budgetary side, the noted tax incentives constitute a "tax expenditure." This means that instead of affirmatively funding the incentive through an exercise of its spending power—for example, by providing a government "match" for all dollars set aside in a favored plan—the incentives come in the form of a reduction or waiver of taxes that a "normal" tax structure suggests the IRS should otherwise collect.¹⁵⁰ In other words, the

but oversimplified, for example, by the failure to take into account the marginal rates at which the \$1,000 will be taxed to each taxpayer in the future upon withdrawal and related time-value of money issues—which are likely to be unknown with any degree of specificity to either taxpayer when the value of the incentive is currently being weighed.

148. Altman, *supra* note 58, at 435; *see also* COMING OF AGE, *supra* note 58, at 21 ("Currently, there is concern that the retirement income system and federal retirement policies are contributing to a two-class system of retirement.").

149. Halperin, *supra* note 121, at 48.

150. *See* Congressional and Budget and Impoundment Control Act of 1974, Pub. L. No. 93-344, § 3(3), 88 Stat. 297, 299 (defining "tax expenditure"). The Joint Committee on Taxation and the Treasury Department each produce annual estimates of the tax expenditures for various matters, although the estimates differ slightly based upon certain underlying assumptions. STAFF OF THE JOINT COMM. ON TAX'N, 107TH CONG., JCS-1-02, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2002–2006 (Comm. Print 2002) [hereinafter JCS-1-02] (providing a detailed discussion of the nature and calculation of tax expenditures), http://www.novoco.com/Legislations/JCT_Tax_Expenditures02-06.pdf (last visited Oct. 12, 2003) (on file with the Washington and Lee Law Review). Indeed, this idea actually is codified in the express purposes underlying ERISA. ERISA, Pub. L. No. 93-406, § 2(a), 88 Stat. 829, 959–64 (codified at I.R.C. §§ 408, 219) ("The Congress finds that . . . employee benefit plans . . . substantially affect the revenues of the United States because they are afforded preferential Federal tax treatment . . ."); 29 U.S.C. § 1001(a) (2000) (same). For an even more recent and detailed treatment of the tax expenditure concept, *see generally* ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2004, at 101–40 (2003), available at <http://www.whitehouse.gov/omb/budget/fy2004/pdf/spec.pdf>. For additional academic treatment of the concept of tax expenditures in the retirement plan context, *see* Altman, *supra* note 58, at 440–42 (discussing tax expenditure concept in context of tax qualified retirement plans); Dilley, *supra* note 66, at 1147 (same); Graetz, *supra* note 58, at 852, 874–75 (same); van Zante, *supra* note 119, at 141–42 (same); Wolk, *supra* note 133, at 422–25 (same).

incentive or "expenditure" is in the nature of foregone tax revenue, which if collected, could then be affirmatively spent in pursuit of encouraging the desired conduct. As a result, the government incurs substantial costs in providing this type of retirement plan tax incentive.¹⁵¹ Moreover, the favorable tax treatment afforded tax-qualified retirement plans constitutes the largest of the tax expenditures, surpassing even the "cost" of the tax breaks granted to homeowners and charitable donors.¹⁵² Because of the great cost to the government, this federal subsidy is justifiable only if it serves some significant public purpose.¹⁵³

As to justification, policymakers defend this tax expenditure on the basis that the federal government has a strong interest in promoting retirement income security.¹⁵⁴ They see the tax code as the best avenue towards achieving the desired end result short of more pervasive paternalism in mandating adequate retirement set asides or a more generous Social Security system.¹⁵⁵ Interestingly, however, Congress specifically employs this inequitable reality—that the tax incentives will be viewed more favorably by higher wage earners—to further leverage the utility of such incentives in the context of employer-sponsored plans. This leverage derives from the operation of the tax-qualification nondiscrimination requirement.¹⁵⁶ Congress designed the

151. See, e.g., Norman P. Stein & Patricia E. Dilley, *Leverage, Linkage, and Leakage: Problems with the Private Pension System and How They Should Inform the Social Security Reform Debate*, 58 WASH. & LEE L. REV. 1369, 1373 (2001) (stating that the retirement plan tax incentive results in \$100 billion in lost tax revenues). For a contrary (and quite ideological) view rejecting the tax expenditure concept, see 147 CONG. REC. S2151 (daily ed. Mar. 12, 2001) (remarks of Sen. Grassley (R-Iowa)) ("I do not buy the philosophy of tax expenditures because that implies every penny working men and women in America earn belongs to the Federal Government and we are going to let them keep some of their own money.").

152. See JCS-1-02, *supra* note 150, at 20–28 (providing tax expenditures for each budget function for Fiscal Years 2002–2006 in table format).

153. See Stein, *supra* note 130, at 225 ("The tax treatment of qualified deferred compensation plans is generally reckoned to give rise to tax expenditures that can be justified only insofar as they contribute to our national retirement policy goals.").

154. ERISA § 2(a) (setting forth in detail the national interest in employee benefit plans); 29 U.S.C. § 1001(a) (same).

155. With regard to paternalism and more universal, mandatory retirement provisions emanating from the federal government, see Altman, *supra* note 58, at 502–08 (discussing the alternatives to the current three-legged stool approach, including expanding Social Security or mandating employer-sponsored pensions); Bankman, *supra* note 73, at 814–27 (discussing paternalism and the forced retirement savings approach to retirement income security).

156. See I.R.C. § 401(a)(4) (2000) (setting forth that one of the requirements of a qualified trust is that the contribution or benefits provided cannot discriminate in favor of highly compensated employees); *id.* § 410(b) (providing the rules for nondiscrimination in coverage); *id.* § 414(q) (stating the definition of a highly compensated employee). A detailed discussion of the nondiscrimination rules is beyond the scope of this Article and has been adequately

requirement "to ensure that [tax-]qualified plans benefit a significant portion of an employer's rank-and-file employees compared to the portion of highly compensated employees benefiting under the plan."¹⁵⁷ The general idea is that higher wage earners will pressure employers to establish tax-qualified plans. The nondiscrimination rules then channel that pressure to inspire more broad-based plans that cover both high and low wage earners, resulting in a more defensible tax expenditure.¹⁵⁸ This nondiscrimination mechanism expressly recognizes the vertical equity shortcomings in the tax incentive approach but then attempts to blunt that distortion through a nondiscrimination tag-along view of who ultimately benefits from the incentives.¹⁵⁹ One should also note that the broad-based employee coverage justification for the tax expenditure does not apply to sole-owner Keogh plans and IRAs because there is no nondiscrimination or other requirement that employees be included in such arrangements.¹⁶⁰ Yet, the tax incentives attendant such devices remain, and the rationale for that discrepancy affects not only considerations of tax equity but also questions about the degree of asset protection that should be afforded the different arrangements.

D. A New Model?

The foregoing explanation of tax incentives and equitable concerns is important to understanding the broader issue of asset protection as it relates to

addressed elsewhere. See, e.g., Altman, *supra* note 58, at 456–70 (discussing pension plan anti-discrimination provisions); Bankman, *supra* note 73, at 795–800 (same); van Zante, *supra* note 119, at 187–202 (same).

157. See JCX-16-99, *supra* note 57, at 8 (explaining the operation of the nondiscrimination rules).

158. Graetz, *supra* note 58, at 887; see Altman, *supra* note 58, at 440 (explaining how tax expenditures are "justified as a mechanism to promote worker security through its ability to induce employers to provide pensions to rank-and-file workers").

159. See Dilley, *supra* note 66, at 1139–42 (noting that the nondiscrimination rules provide a redistributive element to the private pension system, but then discussing ways in which that objective is undercut by other rules). Many have criticized the effectiveness of the tax-incentive "carrot" as coupled with the nondiscrimination "stick" in this regard. See Burke & McCouch, *supra* note 65, at 1249 (noting that the value of the tax incentive depends upon the composition of the workforce as consisting of a sufficient number of high income employees who are willing to channel benefits to low wage earners who place less value on the subsidy); van Zante, *supra* note 119, at 190–91 n.215 (same); see also Altman, *supra* note 58, at 437 ("These [nondiscrimination and integration] rules are outmoded and need to be rethought systematically.").

160. See *supra* notes 135–42 and accompanying text (explaining the tax incentives associated with Keogh plans and IRAs).

retirement income security objectives. Understanding the trust law principles presented in Part II also is helpful because Congress's succinct ERISA anti-alienation mandate left many retirement plan asset protection questions unresolved. For example, with respect to the bulk of private retirement plans, did the seemingly straightforward ERISA anti-alienation language truly represent a third model of asset protection to be defined by its own set of unique policies and goals, or was that mandate merely a specific application and codification of either or both of the Traditional and Self-Settled Models such that traditional concepts come into play where asset protection for retirement arrangements is at issue?¹⁶¹ Part IV of this Article explains how the answers to these alternative questions potentially conflict.

The ambiguity exists because courts have evaluated the creditor-protected status of retirement plan interests at times by reference to traditional spendthrift trust concerns and at other times by straightforward reference to the ERISA anti-alienation mandate.¹⁶² Moreover, the Supreme Court's most significant foray into this arena crafted a landscape in which certain retirement arrangements simply receive blanket protection without further inquiry while others continue to receive careful scrutiny based upon criteria derived from analysis typically ascribed to the Traditional and Self-Settled Models or to exemption laws more generally.¹⁶³

Nevertheless, a decade after this Supreme Court treatment and approaching three decades subsequent to ERISA's enactment, courts and commentators still have difficulty characterizing ERISA's protective mandate. Commentators have described that mandate as "prominent among [ERISA's] . . . provisions"¹⁶⁴ versus a "minor and largely undocumented addition to ERISA."¹⁶⁵ Such dichotomies permeate the federal treatment of this asset protection issue at both the congressional and judicial levels. This treatment evinces an interesting contrast of seemingly scant attention to detail

161. See *supra* notes 40–43 and accompanying text (discussing the distinguishing characteristics of each model).

162. The duplicity in this answer belies the fact that the creditor-protected status of retirement plan interests was at one point noted as "[o]ne of the most hotly litigated issues . . . since the enactment of the [1978] Bankruptcy Code." DANIEL L. KEATING, *BANKRUPTCY AND EMPLOYMENT LAW* § 6.4, at 390 (1995).

163. See *infra* Part IV.B.2 (discussing the holding and implications of *Patterson v. Shumate*, 504 U.S. 753 (1992)).

164. *In re Sewell*, 180 F.3d 707, 710 (5th Cir. 1999).

165. Dilley, *supra* note 35, at 387. Without question, however, the modern impact is pervasive—the DB and DC plan universe alone account for a combined approximately \$4.59 trillion in assets. See JCX-9-02, *supra* note 16, at 34 (noting that DB plans held assets valued at \$2.06 trillion and DC plans held assets valued at \$2.53 trillion as of December 31, 2000).

balanced against occasionally insightful analysis concerning asset protection. The complex maze of laws and plan types that dominate the retirement plan arena makes it no simple task to explore such issues, which continue today to receive considerable judicial attention.¹⁶⁶ Moreover, Congress has now re-entered the foray of creditor-protected retirement plan interests with an approach that carries with it a degree of simplicity in the uniformity of asset protection achieved, though at some cost to equity concerns and perhaps deviating too far from the underlying ERISA objective of promoting retirement income security.¹⁶⁷ Part IV presents these issues more directly through an examination of the apparent reach of the ERISA spendthrift mandate by focusing on both ERISA's technical aspects and the interpretive disagreements that ERISA inspired.

IV. Asset Protection and the Federal Retirement Model

One of the primary sources of confusion in the Federal Retirement Model is the perceived lack of congressional guidance accompanying the adoption of ERISA's dual anti-alienation requirements.¹⁶⁸ Particularly noteworthy is the absence of any overt coordination between this aspect of ERISA and major bankruptcy legislation that followed a few years after ERISA's enactment.¹⁶⁹ The resulting issues have given rise to several distinct progressions in the evolution of the asset protection that defines the Federal Retirement Model. The formative stages of that evolution consistently pulled towards resolving

166. The continuing flow of cases addressing asset protection in the retirement plan context demonstrate the ongoing judicial attention. For examples of such cases, see *infra* notes 227–232.

167. Such matters are discussed in more detail *infra* Part V.

168. The characterization of a "perceived" lack of congressional guidance regarding ERISA and bankruptcy law is intentional, and is intended to give due regard to the "plain language" view reflected in the later judicial analyses that ultimately prevailed in the Supreme Court in *Patterson v. Shumate*, 504 U.S. 753 (1992), as discussed *infra* Part IV.B.2. Notwithstanding the plain language view, courts clearly found themselves adrift in reconciling retirement plan asset protection with the analysis suggested under the Traditional and Self-Settled Models, as evidenced by the federal circuit court split that brought the ERISA spendthrift issue to the Supreme Court.

169. ERISA became effective for plan and tax years beginning after December 31, 1975. ERISA, Pub. L. No. 93-406, § 211(b), 88 Stat. 829, 959–64 (codified at I.R.C. §§ 408, 219); 29 U.S.C. § 1061(b) (2000). Significant portions of the Bankruptcy Code of 1978, now codified in Title 11 of the United States Code, became effective on October 1, 1979. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, §§ 401(a), 402(a), 92 Stat. 2549, 2682. For other indications of congressional inattention to the specifics of retirement plan asset protection, see, for example, *infra* notes 202, 242–246, and accompanying text.

retirement plan asset protection questions by reference to an analysis commonly associated with the Traditional and Self-Settled Models.¹⁷⁰ Through time and judicial decision, however, the analysis has shifted, revealing a Federal Retirement Model that now presents a bifurcated approach to asset protection.¹⁷¹ But, simple bifurcation is an understatement. Further splintering occurs across tax-qualified retirement plan types, all of which are ostensibly designed and rewarded around the unifying theme of promoting retirement income security. Understanding the two key protective mechanisms that may be utilized under the current bankruptcy framework to shield assets is the first step towards appreciating these variations in retirement plan protection.

A. Core Bankruptcy Protections

The Bankruptcy Code of 1978 (the 1978 Code)¹⁷² provides for two basic mechanisms through which debtor assets might be protected from creditor claims—exclusions and exemptions. Both mechanisms play a significant role in the availability of asset protection within the Federal Retirement Model.

1. Exclusion and the Marshalling of Debtor Assets

A key policy goal of the federal bankruptcy system is to marshal debtor assets for use in satisfying creditor claims.¹⁷³ Consistent with this goal, when resolution of a debtor's obligations are subject to a federal bankruptcy

170. See *infra* Part IV.B.1 (discussing in detail the Traditional and Self-Settled Model that courts typically employed in asset protection cases).

171. See *infra* Part IV.B.3 (explaining the ambiguities of the bifurcated approach set forth in *Patterson v. Shumate*, 504 U.S. 753 (1992)).

172. The 1978 Code is codified in Title 11 of the United States Code. *Supra* note 169. The first comprehensive and long-lived bankruptcy legislation in this country was the Bankruptcy Act of 1898, ch. 541, 30 Stat. 544, *repealed* by Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. §§ 101–140)). Although subject to important amendments along the way, the 1898 Act defined the bankruptcy landscape until it was replaced by the 1978 Code. See generally Vern Countryman, *A History of American Bankruptcy Law*, 81 COM. L.J. 226, 228–32 (1976); Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5, 23–37 (1995).

173. This goal competes with the fresh start objective discussed *supra* note 26 and in the text accompanying *supra* note 187. See H.R. REP. NO. 95-595, at 126 (1977), *reprinted in* 1978 U.S.C.A.N. 5963, 6087 ("The historical purpose of [exemption laws] has been to protect a debtor from his creditors, to provide him with the basic necessities of life so that even if his creditors levy on all of his nonexempt property, the debtor will not be left destitute and a public charge.").

proceeding, the bankruptcy court identifies a pool of debtor assets, the "bankruptcy estate," and then oversees the administration of these assets to facilitate the payment of creditor claims.¹⁷⁴ Courts vigorously pursue this goal and broadly interpret the "bankruptcy estate."¹⁷⁵ Consistent with that idea, the 1978 Code expressly nullifies restrictions that purport to limit the transferability of a property interest.¹⁷⁶ Thus, the Code ignores anti-alienation provisions and requires the court to bring the affected interest into the bankruptcy estate for application in satisfaction of creditor claims. However, 1978 Code § 541(c)(2) provides a single statutory exclusion for such interests.¹⁷⁷ Section 541(c)(2) provides that "[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under [the 1978 Code]."¹⁷⁸ Therefore, if a bankrupt debtor is the

174. See 11 U.S.C. § 541(a) (2000) (setting forth the list of assets that comprise the bankruptcy estate); see also *In re Moses*, 167 F.3d 470, 473 (9th Cir. 1999) ("The act of filing a petition under the Bankruptcy Code commences bankruptcy proceedings and creates an estate comprised of [all of the debtor's property]."). If neither the debtor nor any creditors initiate a federal bankruptcy proceeding, the resolution of matters pertaining to satisfaction of the debtor's obligations may be handled as a matter of insolvency under state law. However, given the relevance and preemptive effect of federal bankruptcy laws in this setting, this Article focuses on the federal bankruptcy proceeding as the forum of primary relevance for pursuit of the types of creditor claims that implicate the models discussed here. A similar posture was taken by the commentators in a recent roundtable discussion addressing asset protection trusts. See Symposium, *Roundtable Discussion*, 32 VAND. J. TRANSNAT'L L. 779, 785 (1999) [hereinafter *Roundtable Discussion*] (discussing asset protection trusts and noting that "bankruptcy courts are really going to be the battle grounds on these things"). The focus here is on the bankrupt debtor and the interplay between federal bankruptcy doctrines and relevant state laws, such as the state exemption laws that still pertain in a federal bankruptcy proceeding. Two particular debtor advantages of proceeding under the federal bankruptcy rubric are: (1) the automatic stay, which generally halts all collection efforts and proceedings outside the bankruptcy forum; and (2) the discharge, which generally serves as a release of the debtor (and the debtor's exempt or excluded assets) from liability on all but a handful of specified debts which arose prior to the filing of the bankruptcy petition. See 11 U.S.C. § 362 (stating provisions for the automatic stay); *id.* § 727 (setting forth provisions governing discharge in Chapter 7 proceeding); *id.* § 1328 (setting forth provisions governing discharge in Chapter 13 proceeding); see also John K. Eason, *Developing the Asset Protection Dynamic: A Legacy of Federal Concern*, 31 HOFSTRA L. REV. 23, 53 n.122 (2002) (discussing the advantages of proceeding under federal bankruptcy law as opposed to relevant state laws); *infra* note 178 (stating that the posture of a proceeding under either Chapter 7 or Chapter 13 might make a difference in the debtor's obligations).

175. 11 U.S.C. § 541(a) (2000) provides that property of the bankruptcy estate consists of "all legal or equitable interest of the debtor in property as of the commencement of the [bankruptcy proceeding]."

176. *Id.* § 541(c)(1).

177. *Id.* § 541(c)(2). This provision is hereinafter referred to in the text as "§ 541(c)(2)."

178. *Id.* Whether the proceeding is under Chapter 7 or Chapter 13 of the 1978 Code can make a difference as to the nature of the debtor's obligations in relation to a discharge of pre-

beneficiary of a trust that includes an enforceable spendthrift provision, the debtor's beneficial interest and the underlying property supporting that interest remain beyond the reach of creditors.¹⁷⁹

The resulting protection under § 541(c)(2) appears to be more attributable to ideas of federalism and historical deference to state law recognition of traditional spendthrift trust protections than to either constitutional mandate or any overriding fairness concern.¹⁸⁰ While § 541(c)(2) clearly embodies a rule originally conceived against the backdrop of the Traditional Model, the rule was hardly crafted so as to foreclose more expansive application, and Congress gave little direction in that regard.¹⁸¹ In any event, when the exclusion is

bankruptcy debts, but the exclusion of property has a similarly protective effect in either event. See H.R. REP. NO. 95-595, at 118-26 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6079-87 (discussing the operation of Chapters 7 and 13 of the 1978 Code). For the exclusion of retirement plan interests from the bankruptcy estate under Chapter 7 or Chapter 13 of the 1978 Code, compare *In re Snipe*, 276 B.R. 723, 723-25 (Bankr. D.D.C. 2002) (discussing exclusions under Chapter 13), with *In re Parks*, 255 B.R. 768, 770 (Bankr. D. Utah 2000) (discussing exclusions under Chapter 7).

179. See, e.g., *In re Wilcox*, 233 F.3d 899, 904 (6th Cir. 2000), *cert. denied sub nom. Taunt v. Gen. Retir. Sys. of Detroit*, 533 U.S. 929 (2001) ("An inquiry under § 541(c)(2) normally has three parts: First, does the debtor have a beneficial interest in a trust? Second, is there a restriction on the transfer of that interest? Third, is the restriction enforceable under nonbankruptcy law?"). Similar reasoning has been applied with respect to discretionary trust interests. See, e.g., *In re Blackwell*, 142 B.R. 301, 303 (Bankr. E.D. Ark. 1992) ("Thus, until that [discretionary distribution] decision is made, the pension trust is tantamount to a spendthrift trust such that the property would be excluded from the bankruptcy estate.").

180. As to federalism, see *infra* note 202 regarding references in the legislative history to state spendthrift trust law. On the constitutional issue, see U.S. CONST. art. I, § 8, cl. 4, which confers upon Congress the power to promulgate "uniform laws on the subject of bankruptcies." The noted result with respect to trusts under § 541(c)(2) is consistent with the treatment of such interests under § 70(a)(5) of the 1898 Act, formerly codified at 11 U.S.C. § 110. See DRAFT RESTATEMENT, *supra* note 19, § 58, at 450, Reporter's Notes to cmt. a (noting that 11 U.S.C. § 541(c)(2) "continues a long tradition of giving effect to this particular restriction on transfer"). Under that provision, the excludability of a property interest turned upon its transferability or levability under state law, considered in light of the dual fresh start versus marshalling of assets objectives of the bankruptcy laws. See *In re Goff*, 706 F.2d 574, 578-80 & 581 n.19 (5th Cir. 1983), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992) (discussing spendthrift trust treatment under current § 541(c)(2) and its predecessor under the Bankruptcy Act of 1898); William J. Woodward Jr., *Exemptions, Opting Out, and Bankruptcy Reform*, 43 OHIO ST. L.J. 335, 347 (1982) (explaining that the 1898 Act defined "property of the estate" in terms of transferability or levability under state law). It also has been noted that the general rejection of paying heed to such restrictions "emphasizes the increased independence of the [1978] Code from nonbankruptcy law concerning [what debtor interests constitute] property of the estate." 5 COLLIER ON BANKRUPTCY ¶ 541.24, at 541-99 (Alan N. Resnick & Henry J. Somner eds., 2001) [hereinafter COLLIER].

181. Part IV.B, *infra*, discusses the applicability of the § 541(c)(2) exclusion to interests falling within the Federal Retirement Model. For example, the exclusion would seem to apply to interests falling within the Self-Settled Model, despite the general unavailability of self-

unavailable, debtors must pursue a different avenue to sheltering property from creditor claims in a federal bankruptcy proceeding.

2. *The Exemption Avenue to Preserving a Debtor's Fresh Start*

Exemptions present a second more broadly applicable mechanism for sheltering property otherwise includable in the bankruptcy estate.¹⁸² Operationally, 1978 Code § 522(b)(1) provides that a debtor may exempt property described in a list of federal exemptions set forth in § 522(d) of the 1978 Code, "unless the State law that is applicable to the debtor . . . specifically does not so authorize"¹⁸³ Approximately thirty-five states specifically do not so authorize. In other words, those states have "opted out" of the § 522(d) federal exemption list in accordance with the foregoing language.¹⁸⁴ Section

settled APT protection at the time § 541(c)(2) was enacted, as discussed in the text accompanying *supra* notes 49–55. This exclusion result likely would pertain so long as the bankruptcy court hearing the matter applies the laws of the jurisdiction by reference to which self-settled spendthrift provisions are deemed enforceable. The court's doing so is by no means a foregone conclusion, particularly when the parties or transactions at issue seem more closely related to a non-APT jurisdiction that deems self-settled protection from creditors violative of its public policy. See *supra* note 52 (discussing the problem that arises when the laws of the jurisdiction chosen by the settlor in the trust instrument offend the public policy of the forum state).

182. The exemption issue only arises if no exclusion is available under § 541(c)(2). 11 U.S.C. § 522(b); see S. REP. NO. 95-989, at 82–84 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5868–70 (discussing the various provisions of § 541); see, e.g., *In re Moses*, 167 F.3d 470, 474 (9th Cir. 1999) ("[E]xemption issues only arise if the court concludes that the [property at issue] is part of the bankruptcy estate. In other words, . . . an 'exemption statute' . . . does not effect [property that] . . . is not part of the bankruptcy estate" by virtue of the operation of 11 U.S.C. § 541(c)(2)). The focus of protections shifted from that of exclusions under the 1898 Act to an emphasis upon exemptions under the 1978 Code, although much of the same reasoning applied in both instances. See Wohl, *supra* note 35, at 11 n.48 ("The same analysis that applied to the Bankruptcy Act's notion of includability is appropriate in an analysis of exemption under the Bankruptcy Code.").

183. 11 U.S.C. § 522(b)(1). Section 522(b) of the 1978 Code is hereinafter referred to in the text as "§ 522(b)."

184. In the limited number of states that have not opted-out of the federal exemption scheme, debtors may choose *either* the federal exemptions referenced under § 522(b)(1) and set forth in § 522(d), or the state and nonbankruptcy federal law exemptions described in § 522(b)(2). This further dilutes the impact of the federal exemption scheme under the 1978 Code. See 4 COLLIER, *supra* note 180, ¶ 522.02(1) (discussing the uniform federal exemption list in the context of the states' power to opt out). For a list of the "opt-out" states, see *id.* ¶ 522.01 n.2; see also NAT'L BANKR. REV. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS, FINAL REPORT 299–301 (1997) [hereinafter 1997 FINAL REPORT] (setting forth state-by-state designation of homestead exemption and opt-out status in table form). The 1997 FINAL REPORT reflects the findings of a more recent undertaking to study potential reforms to the federal bankruptcy system.

522(b)(2), in turn, limits debtors residing in one of these "opt-out states" to the exemptions provided under that state's laws plus a handful of exemptions called for under federal laws other than the 1978 Code.¹⁸⁵

The longstanding tenet that exemptions are afforded to debtors for the primary purpose of fostering the greater social good through granting debtors a "fresh start" justifies this protection.¹⁸⁶ The fresh start objective dictates that, notwithstanding bankruptcy, the law should shield certain property from creditor claims so as to provide the debtor with a base of resources sufficient to allow the debtor to pursue a productive lifestyle geared to a more successful financial future.¹⁸⁷ Because such exemptions persist today in the face of the

185. 11 U.S.C. § 522(b)(2). As with the continued recognition of spendthrift restraints in bankruptcy, federal deference to state law as to the particular property to be exempted—maintained through this opt-out exemption scheme—is again attributable to historical and federalism concerns. Congress consistently has rejected calls for uniformity in this regard. For example, Congress created a special Commission on Bankruptcy Laws in connection with pending bankruptcy reform. See S.J. Res. 88, 91st Cong. (1970) (creating a commission to study the bankruptcy laws of the United States). That Commission recommended in its 1973 final report that a set of uniform federal exemptions be adopted in lieu of the state exemption opt-out scheme, but Congress chose to ignore this recommendation. See H.R. DOC. NO. 93-137 (1973), reprinted in B COLLIER, *supra* note 180, Part 4(c), at App. Part 4-421 [hereinafter 1973 Commission Report] ("As a result of the . . . deference to . . . state law as to exemptions, . . . the exemptions available are not the result of reasoned policy but the happenstance of history and location."). The 1973 Commission Report is discussed extensively in *In re Goff*, 706 F.2d 574, 581 n.19 (5th Cir. 1983), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992).

Federal nonbankruptcy laws provide exemptions for Social Security benefits, 42 U.S.C. § 407 (2000), and other federal benefits such as those paid in retirement to civil servants, 5 U.S.C. § 729 (2000). See generally 4 COLLIER, *supra* note 180, ¶ 522.02(3) (listing the benefits exempted under federal nonbankruptcy laws); *In re Goff*, 706 F.2d 574 (5th Cir. 1983) (same). For a discussion of the operation of these federal protections under the 1898 Act, see Vern Countryman, *For a New Exemption Policy in Bankruptcy*, 14 RUTGERS L. REV. 678, 738-40 (1960).

186. This justification pertains whether the exemption is granted under federal law or by virtue of federal deference to state law decisions concerning the specific property exempted.

187. This outcome is in lieu of that debtor becoming a public charge by virtue of "losing everything" to creditors. See H.R. REP. NO. 95-595, at 126 (1977), reprinted in 1978 U.S.C.A.N. 5963, 6087 ("The historical purpose of [exemption laws] has been to protect a debtor from his creditors, to provide him with the basic necessities of life so that even if his creditors levy on all of his nonexempt property, the debtor will not be left destitute and a public charge."); William Houston Brown, *Political and Ethical Considerations of Exemption Limitations: The "Opt Out" as Child of the First and Parent of the Second*, 71 AM. BANKR. L.J. 149, 163-70 (1997) (exploring the purposes underlying bankruptcy exemptions from both a bankruptcy and general perspective); G. Marcus Cole, *The Federalist Cost of Bankruptcy Exemption Reform*, 74 AM. BANKR. L.J. 227, 228 (2000) (noting that the fresh start objective is a "central justification for a consumer bankruptcy system. Productive but unfortunate individuals might decline to contribute to society if the benefits of their productive energies were completely captured by past creditors." (citations omitted)); see generally William T. Vukowick, *Debtor's Exemption Rights Under the Bankruptcy Reform Act*, 58 N.C. L. REV. 769

competing federal bankruptcy policy of liberally marshalling the debtor's assets, the exemptions demonstrate the efficacy of this fresh start objective and its concern for the debtor's long-term financial recovery and well-being. Interestingly, however, no such justification rises to the forefront when one examines the *exclusion* under § 541(c)(2).¹⁸⁸ This dichotomy is merely one of the many inconsistent asset protection rules affecting the Federal Retirement Model, as explored next.

B. ERISA's Attendant Questions and Conflicts

Prior to ERISA's enactment, retirement plan interests and assets found protection from creditors through state exemption laws and a degree of deference under the Bankruptcy Act of 1898 to pre-ERISA anti-alienation provisions applicable to some plans.¹⁸⁹ More specifically, if the debtor's interest in a retirement plan was neither transferable nor leviable under state laws, as was often the case when an anti-alienation provision applied, then the 1898 Act excluded the interest from the bankruptcy estate and thus protected the interest from creditor claims.¹⁹⁰ Not surprisingly, the resulting association of such plans with spendthrift trusts raised questions about the protected status of retirement plan interests, particularly given that many courts characterized such interests as self-settled arrangements.¹⁹¹ One court described this

(1980) (discussing a debtor's exemption rights in the context of § 522 of the Bankruptcy Act of 1978).

188. In fact, Congress specifically rejected limiting the § 541(c)(2) exclusion to any defining standard that would have tied the offered protection to some concept of need. See *infra* notes 244–48 and accompanying text (stating that both Houses rejected the "reasonably necessary" cap on the amount to be protected from creditors under the § 541(c)(2) exclusion).

189. See Jeffrey R. Houle, *ERISA-Qualified Pension Plans as Property of the Bankruptcy Estate: A Survey of Creditor's Rights to Participants' Pension Assets Pre- and Post-Patterson v. Shumate*, 29 HOUS. L. REV. 763, 773–75 & n.60 (1992) (discussing the status of retirement plan assets under pre-ERISA law); Seiden, *supra* note 35, at 231–34 & nn.59–60, 74–76 (describing results under § 70(a)(5) of the 1898 Act both before and after the enactment of ERISA and citing relevant cases); Wohl, *supra* note 35, at 6–11 (discussing the status of retirement assets prior to 1978 Code). With regard to the 1898 Act, see *supra* notes 172 and 180 and accompanying text.

190. See *infra* notes 230–31 regarding the potential non-ERISA sources of a retirement plan anti-alienation provision. See *supra* note 180 regarding § 70(a)(5) of the 1898 Act, the precursor to 1978 Code § 541(c)(2). For cases discussing retirement plan asset protection under the 1898 Act, see *In re Graham*, 726 F.2d 1268, 1271 (8th Cir. 1984), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); *In re Goff*, 706 F.2d 574, 578 (5th Cir. 1983), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); *In re Baviello*, 12 B.R. 412, 414–15 (Bankr. E.D.N.Y. 1981).

191. See *supra* note 55 and *infra* notes 212–13 and accompanying text regarding the self-

retirement plan asset protection situation as presenting an "analytical conundrum."¹⁹² This conundrum prompted yet another court to note that "every lawyer who counseled debtors under [the 1898 Act] knows the question of whether bankrupts kept their pension rights was a mess under the transferability-leviability standard."¹⁹³

Against this backdrop, Congress enacted ERISA and its "terse" but mandatory anti-alienation provisions.¹⁹⁴ By doing so, Congress "dramatically increased the pension plan interests which courts could exclude" from creditor claims under the 1898 Act.¹⁹⁵ Logic suggests that Congress intended to protect retirement interests by bringing them more clearly within the ambit of asset protection standards governing such matters at the time. The legislative history of the ERISA anti-alienation mandate is brief, however, and includes only a general statement of purpose to ensure that pension assets remained available for retirement use.¹⁹⁶ Some explain the lack of any meaningful treatment of the anti-alienation requirements in the legislative history of ERISA as "doubtless on the ground that the [overriding] purpose is too obvious for words."¹⁹⁷ Nevertheless, Congress caused confusion because it provided no insight on such matters as the continued relevance of the self-settled nature of many retirement arrangements or the necessity of a connection between such interests and a debtor's fresh start needs. These uncertainties led others to conclude that "[c]learly, Congress has not thought the issue through."¹⁹⁸ Moreover, this perceived lack of congressional attention to detail regarding retirement plan

settled nature of many retirement plans.

192. *In re Goff*, 706 F.2d at 578.

193. *In re Threewitt*, 20 B.R. 434, 437 (Bankr. D. Kan. 1982) (quoting Doug Rendleman, *Liquidation Bankruptcy Under the '78 Code*, 21 WM. & MARY L. REV. 575, 597 (1980)), *rev'd*, 24 B.R. 927 (D. Kan. 1982). For a recitation of the various outcomes under the 1898 Act and prior to the enactment of ERISA, see the case summaries found in Houle, *supra* note 189, at 774-75 n.60. Houle notes that "[u]nder pre-Bankruptcy Code law, exclusion of plan benefits from the owner-employee's bankruptcy estate was unsettled." Houle, *supra* note 189, at 775 n.60; see also Seiden, *supra* note 35, at 233-34 & nn.74-76 (describing results under § 70(a)(5) of the 1898 Act both before and after the enactment of ERISA and citing relevant cases).

194. See *In re Goff*, 706 F.2d at 585 n.28 (describing ERISA's anti-alienation provisions as "terse recitations").

195. Houle, *supra* note 189, at 775-76.

196. The only significant legislative history concerning ERISA's anti-alienation requirements indicates that the provision was adopted in order "[t]o further ensure that the employee's accrued [sic.] [retirement plan] benefits are actually available for retirement purposes." H.R. REP. NO. 93-807, at 65 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4670, 4734.

197. LANGBEIN & WOLK, *supra* note 90, at 575.

198. Jeffrey G. Sherman, *Spendthrift Trusts and Employee Pensions: The Problem of Creditors' Rights*, 55 IND. L.J. 247, 271 (1980).

asset protection became a glaring source of disagreement following the enactment of the 1978 Code.¹⁹⁹ Thereafter, retirement plan asset protection analysis rested on the alternative protective mechanisms of exclusion under the 1978 Code § 541(c)(2) and exemption under § 522(b).²⁰⁰ Questions concerning the proper application of each concept to retirement plan interests left courts groping to define the rules of asset protection under the Federal Retirement Model.

The overriding problem lies in the inherent conflict between the bankruptcy policies of marshalling assets for creditors subject to a debtor's fresh start needs versus the basic tenet of federal retirement policy that encourages workers to set aside funds currently in order to facilitate a more secure retirement.²⁰¹ Such future retirement needs most often implicate considerations spanning beyond the immediacy of a fresh start. The more specific problem is the original failure by Congress to grasp this conflict between ERISA and the 1978 Code or, at best, to foresee, or at least forestall, the interpretive issues that would almost certainly arise under the framework established.²⁰² In particular, divergent possibilities for the evolution of asset protection within the Federal Retirement Model found roots in the congressional preservation under 1978 Code § 541(c)(2) of creditor-protection provided through a valid spendthrift restraint.²⁰³ Though this concept may

199. The 1978 Code replaced the prior Act's transferability/leviability test with a broad marshalling of debtor assets concept, as discussed in the text accompanying *supra* notes 173–75. The transferability/leviability test is discussed in *supra* note 180 and the accompanying text. See Houle, *supra* note 189, at 773–74 (noting that the 1978 Code created conflict between ERISA and bankruptcy laws). Regarding the policy of marshalling debtor assets for application in payment of creditor claims, as pursued under the 1978 Code, see *supra* notes 173–175 and accompanying text.

200. See Part IV.A (discussing bankruptcy exemptions and exclusions).

201. See, in this regard, the legislative history of ERISA § 206(d)(1), discussed *supra* note 196, and the Third Circuit's explanation of the issue as quoted in the text accompanying *infra* note 208. See also KEATING, *supra* note 162, § 6.4.1 (noting the different arguments a debtor could make in an attempt to exclude pension assets from the bankruptcy estate). The dual fresh start and marshalling of assets policies are discussed *supra* Part IV.A.

202. There were other legislative gaps as well, including: (1) isolated reference in the legislative history of § 541(c)(2) to only "state" spendthrift trust laws, as explained in *In re Goff*, 706 F.2d 574, 580–82 (5th Cir. 1983), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); (2) the lone reference by Congress to retirement plan interests as meriting a federal exemption under § 522(d)(10)(E) of the 1978 Code, as discussed *infra* notes 235–255; (3) the lack of any reference to ERISA in the supplemental exemptions granted by "other federal law" under § 522(b)(2)(A) of the 1978 Code, as noted in *In re Dyke*, 943 F.2d 1435, 1444–45 (5th Cir. 1991), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); and (4) the complete absence of any other express coordination of the competing bankruptcy and retirement policies in the 1978 Code or its legislative history.

203. See Part IV.A.1 regarding § 541(c)(2) as it pertains to spendthrift restraints.

seem simple in light of the ERISA anti-alienation mandate, Congress meted out several avenues for interpretive uncertainty.

The primary source of disagreement lay in the text of § 541(c)(2) itself, which provides that an anti-alienation restraint on the transfer of a debtor's beneficial trust interest that is "enforceable under applicable nonbankruptcy law" is likewise enforceable in bankruptcy.²⁰⁴ The specific question presented was whether ERISA constituted "applicable nonbankruptcy law," such that a retirement plan interest subject to an ERISA-mandated anti-alienation provision would be immune from creditor attachment.²⁰⁵ More generally, for almost twenty years after ERISA's enactment, divergent perspectives as to the meshing of bankruptcy law, traditional and self-settled spendthrift trust law, and ERISA clouded progressions in the development of the Federal Retirement Model.²⁰⁶ As discussed next, the resulting tensions ultimately produced two distinct progressions in the analysis governing the question of retirement plan asset protection and several important inconsistencies in that protection still remain.

1. The Initial Stage of Post-ERISA Protection

The post-ERISA evolution of retirement plan asset protection originates in the question of whether the ERISA anti-alienation mandate truly presented something unique. Specifically, did ERISA present a new model of asset protection, or did ERISA simply fit neatly within the Traditional and Self-Settled Models that came before it, perhaps distinguishable only in that in some instances "the courts [might] be called upon to fashion a federal common law of spendthrift trusts in connection with employee pension plans?"²⁰⁷ The Third

204. See *supra* notes 177–79 and accompanying text (discussing the statutory exclusion under § 541(c)(2)).

205. As pointed out in *supra* note 202, the only references in the legislative history of § 541(c)(2) on this language pertained to "state" spendthrift trust laws.

206. See *Velis v. Kardanis*, 949 F.2d 78, 79 (3d Cir. 1991) ("[T]he reported decisions are in disarray, as to whether 'applicable nonbankruptcy law' in this context was intended by Congress to be limited to state spendthrift trust law, or whether it embraces federal law as well.").

207. Sherman, *supra* note 198, at 260–61; see also Michael J. Collins, *The Federal Common Law of ERISA*, 59 N.Y.U. INST. ON FED. TAX'N 16-1, 16-2 (Supp. 2001) ("[C]ourts are often tempted to address what they believe must be oversights in the [ERISA] statutory scheme by invoking the federal common law of ERISA."); Seiden, *supra* note 35, at 233 ("If the plan or trust contained a valid spendthrift clause, then the plan interest was not property of the estate [A]fter the enactment of ERISA, some courts looked to ERISA to determine whether the interest was transferable [sic]." (footnote omitted)). Of course, the actual issue most often was the fitting of a retirement trust within the bounds of existing state spendthrift trust law. See David B. Young, *The Pro Tanto Invalidity of Protective Trusts: Partial Self-*

Circuit captured this conceptual "nothing new/something unique" dichotomy in its assessment of the ERISA, bankruptcy, and federalism contrasts presented:

It is argued [on the one hand] that Congress cannot have intended to enable persons to place their assets beyond the reach of creditors by placing [such assets] in a trust for [such persons'] own benefit, except to the limited extent that the laws of the various states would uphold the spendthrift provisions But [on the other hand] there can be no doubt that Congress has expressed a deep and continuing interest in the preservation of pension plans, and in encouraging retirement savings, as reflected in the statutes which have given us ERISA²⁰⁸

Perhaps not surprisingly, then, the circuit courts considering whether an ERISA spendthrift retirement plan interest deserves asset protection split along lines consistent with these possibilities. One primary viewpoint held that the reference in § 541(c)(2) to "applicable nonbankruptcy law" was limited to state spendthrift trust law, meaning that retirement plan interests could be excluded from the bankruptcy estate only if they qualified for protection by virtue of analysis consistent with that discussed above in the context of the Traditional and Self-Settled Models.²⁰⁹ But another competing viewpoint held that such plan interests were straightforwardly excluded from the bankruptcy estate under § 541(c)(2) of the 1978 Code by virtue of the ERISA anti-alienation mandate as constituting "applicable nonbankruptcy law" within the "plain language" of § 541(c)(2).²¹⁰

Settlement and Beneficiary Control, 78 MARQ. L. REV. 807, 825–26 (1995) ("This was an instance of difficult cases frequently leading to harsh and confusing results. Relatively few state court cases had dealt with retirement trusts in this light" (footnotes omitted)).

208. *Velis*, 949 F.2d at 82.

209. See, e.g., *In re Reed*, 951 F.2d 1046, 1050 (9th Cir. 1991) (holding that ERISA is not "applicable nonbankruptcy law," and that pension interest at issue failed as a spendthrift trust under applicable state law), *vacated sub nom. Reed v. Drummond*, 506 U.S. 910 (1992); *In re Lichstrahl*, 750 F.2d 1488, 1490 (11th Cir. 1985) (same), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992); *In re Graham*, 726 F.2d 1268, 1272–73 (8th Cir. 1984) (same), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992); *In re Goff*, 706 F.2d 574, 582 (5th Cir. 1983) (same), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992); *Regan v. Ross*, 691 F.2d 81, 84 (2d Cir. 1982) (concluding that ERISA does not constitute "applicable nonbankruptcy law"). See generally *In re Lucas*, 924 F.2d 597, 600–02 (6th Cir. 1991) (discussing divergent judicial opinions under theories (1) and (2) as noted in the text, *supra*, and holding that ERISA is not "applicable nonbankruptcy law"). The standard analysis under the Traditional and Self-Settled Models is discussed *supra* Part II.

210. See, e.g., *In re Moore*, 907 F.2d 1476, 1478–79 (4th Cir. 1990) (adopting a "plain language" interpretation and finding that ERISA constituted "applicable nonbankruptcy law" pursuant to which a pension plan spendthrift provision resulted in exclusion of the interest from the bankruptcy estate). Adoption of this view by the Supreme Court in 1992 ushered in what is characterized here as the second major progression in the analysis of retirement plan asset protection, as discussed *infra* Part IV.B.2.

Most courts considering the matter prior to 1990 adopted the first noted view of ERISA protection.²¹¹ Specifically, those courts held that the creditor-protected status of retirement plan interests presented an evolutionary path for the Federal Retirement Model that left the model ensconced within the framework of traditional spendthrift trust principles, subject to the caveat that self-settled or other beneficiary-controlled spendthrifted arrangements were not shielded in the face of a creditor challenge.²¹² Although a court could

When neither of the theories set forth in the text supported the debtor's call for exclusion, that debtor had to seek to protect the retirement plan interest as property that, although included in the bankruptcy estate, was nevertheless shielded from creditors under the ambit of some specific exemption law. The three primary theories in this regard deferred to: (1) the federal exemption found in 11 U.S.C. § 522(d)(10)(E) of the 1978 Code, as discussed in *Velis*, 949 F.2d at 81–82 and *infra* notes 235–55; (2) state law exemptions pertaining specifically to retirement plan interests, as discussed in *In re Dyke*, 943 F.2d 1435, 1438–40 (5th Cir. 1991), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992); or (3) the supplemental exemption under 11 U.S.C. § 522(b)(2)(A) of the 1978 Code. The latter provision permits debtors proceeding under a state law exemption scheme to also exempt property specified under "other federal law," meaning federal law that is not embodied in the 1978 Code. Although ERISA seemingly meets that description, however, it was generally held that the reference to federal law in 11 U.S.C. § 522(b)(2)(A) did not intend to include ERISA. *See, e.g., In re Dyke*, 943 F.2d at 1444–46 (discussing judicial decisions on this issue and ultimately holding, as have most courts, that ERISA did not constitute "other federal law" as contemplated under 11 U.S.C. § 522(b)(2)(A)); *In re Graham*, 726 F.2d at 1274 (reaching the same conclusion), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992). In this regard, note that while the legislative history of 11 U.S.C. § 522(b)(2)(A) enumerated many federal laws as contemplated to fall within that provision, ERISA was not on the list. S. REP. NO. 95-989, at 75 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5861; H.R. REP. NO. 95-595, at 360 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6316. In dealing with this issue, the Eighth Circuit noted that "the provisions of some of the statutes on the list creating a federal exemption are similar to the anti-alienation provisions of ERISA," but then concluded that "[t]he pensions . . . in the illustrative list are all peculiarly federal in nature." *In re Graham*, 726 F.2d at 1274. Although the § 522(b)(2)(A) "other federal exemption" argument met little success at the circuit court level, lower federal courts reached "diametrically opposite interpretations of the scope of this provision relative to ERISA-qualified pension plans." *In re Goff*, 706 F.2d at 583, *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992). For a discussion of the five theories advanced by debtors prior to *Shumate* in arguing that plan assets are beyond the reach of creditors, see JCS-16-91, *supra* note 35, at 6–8.

211. This view was the majority among federal circuits courts of appeal until a rash of decisions immediately preceding *Patterson v. Shumate* rendered the split more even. *See Patterson v. Shumate*, 504 U.S. 753, 757 n.1 (1992) (discussing the courts of appeals decisions); *In re Dyke*, 943 F.2d at 1441 (discussing cases), *abrogated by Patterson v. Shumate*, 504 U.S. 753 (1992); *Velis*, 949 F.2d at 80–81 (same). The Fourth Circuit decision in *In re Moore* was the first federal circuit court decision to reject the spendthrift trust analysis and hold that the "plain language" of 11 U.S.C. § 541(c)(2) encompassed ERISA's anti-alienation mandate as "applicable nonbankruptcy law." *In re Moore*, 907 F.2d at 1478–79.

212. In other words, the ERISA anti-alienation clause would protect the retirement interest unless state law considerations such as self-settlement or too much debtor access to and control over the retirement fund dictated otherwise. *See, e.g., In re Reed*, 951 F.2d at 1050 (holding

characterize most retirement plans as at least nominally self-settled because funding is provided directly by the employee or in exchange for the employee's efforts, most courts were lenient in this regard, at least with respect to required employee contributions and employer contributions paid in consideration for work performed.²¹³ Therefore, the distinction between valid and invalid arrangements tended to focus on voluntary debtor contributions and most often

that ERISA is not "applicable nonbankruptcy law," and that pension interest at issue failed as a spendthrift trust under applicable state law), *vacated sub nom.* *Reed v. Drummond*, 506 U.S. 910 (1992); *In re Litchstrahl*, 750 F.2d at 1490 (same), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); *In re Goff*, 706 F.2d at 589 (same), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992). *See generally In re Lucas*, 924 F.2d at 600-02 (discussing divergent judicial opinions under theories (1) and (2) as noted in the text, *supra* notes 209-10, and holding that ERISA is not "applicable nonbankruptcy law"). *But see In re Graham*, 726 F.2d at 1272-73 ("The question of pension rights is dealt with as a matter of exemption."), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992); *Regan v. Ross*, 691 F.2d 81, 86 (2d Cir. 1982) (stating a similar conclusion). *See generally* PETER SPERO, ASSET PROTECTION LEGAL PLANNING STRATEGIES § 10.04(2)(d) (1994) (discussing spendthrift protecting and self-settled trust); Young, *supra* note 207 states:

The general rule in the employee retirement trust cases, then, was that an ERISA-qualified plan would be upheld *in toto* as a valid spendthrift trust if: (1) the employer had funded the entire plan; and (2) the debtor-beneficiary was a mere wage employee with no significant equity ownership in or right of control over the employer. Conversely, a plan would be held totally self-settled if either: (1) the beneficiary enjoyed significant ownership and control over the employer; or (2) the employee had in fact funded the entire trust out of her own pocket.

Id. at 831.

213. *See In re Idalski*, 123 B.R. 222, 225-26 (Bankr. E.D. Mich. 1991) (discussing cases where either the employer's contributions in consideration for work or the employee's non-voluntary contribution wholly funded employee benefit plans); SPERO, *supra* note 212, § 10.04(2)(d) (providing an overview of cases and concluding that "the overwhelming weight of authority is [that] . . . [t]rusts have not been treated as self-settled merely because mandatory contributions were made . . . and where deferred compensation was negotiated by the debtor with his employer." (footnotes omitted)). The argument for self-settled status by virtue of the employee's work efforts is summarized nicely in *Legal Problems of Private Pension Plans*, *supra* note 55:

The employee is a settlor to the extent that his interest is attributable to his contributions. If employer contributions are considered compensation for which the employee has given consideration, the employee would seem also to be the settlor as to these amounts. Thus, only if the pension is considered a gift which confers no property interest on the employee or if the courts exempt pensions from the normal trust rule on grounds of public policy can an employee's interest be kept from his creditors.

Id. at 499; *see also* IIA SCOTT & FRATCHER, *supra* note 18, § 156.3, at 185 (noting that employment trusts are arguably self-settled in that "the trust is created in consideration of services rendered by the employees, and that the employees are therefore the settlors"); Young, *supra* note 207, at 825-36 (discussing cases pertaining to the self-settled nature of retirement trusts).

turned on matters of debtor access to and control over the retirement plan assets.²¹⁴

Although matters of source-of-funds self-settlement were relevant, the crux of this analysis ultimately focused upon the reality of the spendthrift nature of the retirement plan interest at issue. In other words, if debtor control or withdrawal powers rendered the anti-alienation mandate one in form only, then no clear purpose akin to that motivating the spendthrift of property existed so as to justify shielding the interest from creditors.²¹⁵ In the retirement plan context, the alleged justification is that of preserving assets for retirement uses—a purpose that is not served when ready access to and control over the fund for which protection is sought renders that fund available for nonretirement-related consumption.²¹⁶ This observation, derived from the

214. See, e.g., *In re Moses*, 167 F.3d 470, 473 (9th Cir. 1999) (discussing self-settled trust and debtor access/control issues in relation to pension plan protection under state spendthrift trust laws, and finding both characteristics lacking under separate and distinct analyses); *In re Dyke*, 943 F.2d at 1444 ("[A] beneficiary who enjoys 'access to and control over' a pension plan is a settlor of the plan, even though another person or entity nominally created the plan." (quoting *In re Brooks*, 844 F.2d 258, 263 (5th Cir. 1988))); *In re Kincaid*, 917 F.2d 1162, 1167–68 (9th Cir. 1990) (concluding that a retirement plan was a spendthrift trust after determining that the trust was not self-settled, and that debtor had only restricted access to the funds); *In re Moore*, 907 F.2d 1476, 1478 (4th Cir. 1990) (adopting a "plain language" construction of 11 U.S.C. § 541(c)(2), but nevertheless distinguishing earlier cases applying state spendthrift trust law on the ground that "here, the beneficiaries do not control the plan, cannot make unrestricted withdrawals from it, cannot borrow against it, and cannot amend it"); see also Houle, *supra* note 189, at 816–17 (discussing analysis under enforceable spendthrift trust criteria as combining factors of debtor funding, access, and control); Wohl, *supra* note 35, at 33 ("The primary reason courts have been unwilling to treat pension trusts as spendthrift trusts . . . is . . . that pension assets . . . can [be] reduce[d] to possession . . . immediately after the termination of the bankruptcy proceedings.").

215. See, e.g., *In re Dyke*, 943 F.2d at 1444 ("Not all ERISA-qualified retirement plans . . . are spendthrift trusts: Those retirement plans which are self-settled do not qualify. And in particular, if the beneficiaries of a plan enjoy access to and control over the funds in the plan, then the plan is not a spendthrift trust."); *In re Lichstrahl*, 750 F.2d 1488, 1490 (11th Cir. 1985) (noting, in denying protection to debtor-controlled pension plans that "[t]he reasons for creating and enforcing spendthrift trusts would not be served if we were unwilling to look beyond legal forms"), *abrogated by* *Patterson v. Shumate*, 504 U.S. 753 (1992). For a post-*Shumate* application of this analysis, see Part IV.B.

216. See the legislative history of ERISA § 206(d)(1) at *supra* note 196 and see the discussion of "leakage" at *infra* notes 286–87 and the accompanying text. See Dilley, *supra* note 35, at 389 (discussing the rationale behind the 1978 bankruptcy legislation); Houle, *supra* note 189, at 813 (noting the difference between ERISA trust pension plans and ERISA savings account pension plans, specifically regarding debtor access); see also Jefferson, *supra* note 136, at 1456 (decrying evolution of IRAs from retirement-directed arrangements to more general tax-preferred savings plans not necessarily destined for retirement uses).

Paradoxically, however, in most instances the debtor's access and control are grounded in the federal laws which established the retirement arrangement with the blessing of favorable tax treatment, ostensibly for purposes of retirement in lieu of current consumption. This realization

original application of spendthrift trust principles to retirement plans, is important. It suggests that asset protection for retirement plans should be fundamentally grounded in service to the overriding goal upon which that protection is granted—namely, the goal of retirement income security for citizens.

2. *Patterson v. Shumate and the Second Progression in Retirement Plan Protection*

But, in lieu of pursuing this policy-based analysis and the resolution offered under longstanding trust principles, the Supreme Court chose a different path. In *Patterson v. Shumate*,²¹⁷ the Court subordinated the early push to graft such considerations upon the development of the Federal Retirement Model, and instead adopted the "plain language" view of ERISA asset protection noted above.²¹⁸ The Court held that the § 541(c)(2) exclusion encompassed the ERISA anti-alienation mandate and was not limited to protecting spendthrift trusts under state law.²¹⁹ The Court summarily dismissed

and its proper place in the asset protection analysis is discussed in detail *infra* Part V. With regard to those federal laws and by way of example, both the employer and employee contributions can be withdrawn from a profit sharing or stock bonus plan (each subject to both the labor and tax anti-alienation provisions of ERISA) generally after two years or upon certain other events which may or may not relate to retirement. Treas. Reg. § 1.401-1(b)(1) (1988); JCX-16-99, *supra* note 57, at 18. Although certain other types of plans may purportedly be subject to more restrictive rules in this regard, employee contributions and the earnings attributable thereto often may be withdrawn from such arrangements for reasons entirely unrelated to retirement. See 2 BITTKER & LOKKEN, *supra* note 123, § 61.12.2 (discussing restrictions on early distributions from retirement plans). Taxable amounts withdrawn before the employee-participant reaches age 59½ are generally subject to a 10% penalty tax, which many courts regard as an insufficient penalty to negate the employee's control and access. See I.R.C. § 72(t) (2000) (imposing 10% penalty on early distribution from qualified retirement plans); *In re Goff*, 706 F.2d 574, 589 (5th Cir. 1983) (finding 10% penalty insufficient to negate debtor control and access); *supra* note 48 (discussing federal laws regulating access to funds in retirement plans).

217. *Patterson v. Shumate*, 504 U.S. 753, 759–60 (1992).

218. See *supra* note 210 and accompanying text regarding the "plain language" view.

219. The facts, arguments and holding in *Patterson v. Shumate* have been analyzed extensively in subsequent judicial decisions and academic literature, and will be addressed here only to the extent that doing so sheds light upon the perspective pursued in this Article. The case involved a plan that was subject to both the labor and tax ERISA spendthrift mandates and as to which the debtor had significant control over the plan. *Shumate*, 504 U.S. at 762–63. The court held that the plan was excluded from the bankruptcy estate by virtue of § 541(c)(2), without precisely clarifying the scope of its decision and with no mention of the control issue. *Id.* at 760. For a good judicial overview of the decision, see *In re Moses*, 167 F.3d at 475. That the Supreme Court ultimately resolved this matter by reference to the "plain language" of 11

the alternative view espoused in prior lower court decisions that relied upon the legislative history of the 1978 Code to equate the bankruptcy exclusion of affected ERISA retirement plan interests with state spendthrift trust law and analyses.²²⁰ This dismissal seemingly forestalled further policy-based inquiry into the balancing of competing legislative objectives and the proper placement of retirement plan interests relative to the protections offered through the Traditional and Self-Settled Models.²²¹ Stated simply, such interests were uniquely entitled to exclusion from the bankruptcy estate without further

U.S.C. § 541(c)(2) of the Bankruptcy Code does not belie the premise posited above—that a lack of clarity in the congressional edicts left open the nature and parameters of the Federal Retirement Model—as attested to by the divergence of judicial opinions leading up to the 1992 decision. Rather, that divergence of opinion is indicative of the intimate tie between the interests and creditor opportunities at issue, with the Supreme Court finally stepping in to cast certain retirement plan interests in a unique light.

220. See *Shumate*, 504 U.S. at 761 n.4 ("The Courts of Appeals that have limited 'applicable nonbankruptcy law' to state spendthrift trust laws by ignoring the plain language of § 541(c)(2) and relying on isolated excerpts from the legislative history thus have misconceived the appropriate analytical task."); *Shumate v. Patterson*, 943 F.2d 362, 363–64 (4th Cir. 1991) ("[The district court's] focus on state spendthrift trust law, which looks to the reality behind the non-alienation provision, is misplaced."), *aff'd*, 504 U.S. 753 (1992); see also *In re Wilcox*, 233 F.3d 899, 904 (6th Cir. 2001) (holding that subsequent to *Patterson v. Shumate*, analysis of the exclusion of a pension plan interest under 11 U.S.C. § 541(c)(2) by reference to state spendthrift trust rules, and in particular those pertaining to self-settled trusts, was error), *cert. denied sub nom. Taunt v. Gen. Retirement Sys. of Detroit*, 533 U.S. 929 (2001); *In re Meehan*, 102 F.3d 1209, 1213 (11th Cir. 1997) (stating that the *Shumate* decision implicitly forecloses state spendthrift trust law analysis of a retirement plan interest that is subject to an anti-alienation provision enforceable under nonbankruptcy law, such as ERISA or corresponding state law, and that debtor's control over the retirement plan is thus a nonissue with respect to such plans). But see *In re Baker*, 114 F.3d 636, 638 (7th Cir. 1997) ("We do not read [*Shumate*] to say that money readily available to participants for current consumption necessarily is unavailable to repay debts But . . . we do not pursue the question." (citation omitted)). With regard to the legislative history of 1978 Code § 541(c)(2) referencing both "applicable state law" and "applicable nonbankruptcy law," see H.R. REP. NO. 95-595, at 176, 369 (1977), *reprinted in* 1978 U.S.C.A.N. 5963, 6136, 6325, as discussed in *In re Moore*, 907 F.2d 1476, 1479 (4th Cir. 1990).

221. The competing legislative objectives were those underlying the broad marshalling of assets in bankruptcy, versus the broad protection for such assets under ERISA. Without expressly mentioning the 1978 Code's dual marshalling of assets/fresh start concerns, the *Shumate* Court also noted that the 1978 Code's broad definition of "property," as reflected in 1978 Code § 541(a), fell short of a "policy" that was in any way conflicted with ERISA on the question of excluding retirement plan assets from the bankruptcy estate. See 11 U.S.C. § 541(a) (2000) (defining a bankruptcy estate); *Shumate*, 504 U.S. at 763–64 ("[W]e think that petitioner mistakes an admittedly broad definition of includable property for a 'policy' underlying the [Bankruptcy] Code as a whole."); see also *In re Whetzal*, 32 F.3d 1302, 1304 (8th Cir. 1994) ("[T]he Court [*in Shumate*] emphasized its view that the more important policy is protecting pension benefits."). *Supra* Part IV.A discusses the bankruptcy estate concept, marshalling of assets, and fresh start policies. *Supra* note 175 sets forth § 541(a) of the 1978 Code.

deference to other policy concerns. In fact, the Court adhered to its earlier espoused view that ERISA policies were to be regarded as pre-eminent to creditors' rights.²²² *Shumate* thereby ushered in the second progression in the evolution of the Federal Retirement Model, by establishing certain retirement plan interests as deserving unique, unilateral protection from creditors in bankruptcy via § 541(c)(2).

3. Bifurcation in the Post-Shumate Analysis

The apparent simplicity of blanket asset protection for plans that *Shumate* covers, however, is deceptive. The line of demarcation between covered and exposed plans is elusive. This unclear line of demarcation arises from the ambiguous language chosen by the *Shumate* Court to articulate its specific holding that "a debtor's interest in an *ERISA-qualified* pension plan may be excluded from the property of the bankruptcy estate pursuant to § 541(c)(2)."²²³ This "ERISA-qualified" phraseology has given rise to perhaps as many new questions as it purported to resolve, and the further analysis undertaken to answer that question has dominated post-*Shumate* developments in the Federal Retirement Model. As the Fifth Circuit recently stated, the *Shumate* "Court inadvertently opened another jurisprudential Pandora's Box" regarding the import of the ERISA anti-alienation requirement in the seminal battleground of bankruptcy.²²⁴ The confusion lies in the fact that "qualified plan" is a term commonly utilized as a reference to *tax-qualification* in the context of retirement plans, whereas the Court's chosen "ERISA-qualified" terminology finds life in neither statute nor common parlance, though it might seem to suggest tax qualification.²²⁵ Perhaps unwittingly, the Court focused attention

222. See *Guidry v. Sheet Metal Workers Nat'l Pension Fund*, 493 U.S. 365, 374–76 (1990) (declining to create an exception to ERISA's prohibition on the blank of pension funds). In *Guidry*, the petitioner embezzled funds from the union, and the lower courts imposed a constructive trust on his pension plan benefits in favor of the union. *Id.* at 365. The Supreme Court ultimately rejected this outcome on the strength of ERISA's § 206(d)(1) mandate. *Id.* In so holding, the Court deferred to the overriding importance of ERISA's retirement income security objective, noting "that the effectuation of certain broad social policies sometimes takes precedence over the desire to do equity between particular parties." *Id.* at 376.

223. *Shumate*, 504 U.S. at 765 (emphasis added).

224. *In re Sewell*, 180 F.3d 707, 711 (5th Cir. 1999); see also *In re Baker*, 114 F.3d at 638 ("What is an 'ERISA-qualified' plan? The term does not appear in the statute, and its provenance is mysterious.").

225. See *In re Sewell*, 180 F.3d at 711–12 ("[ERISA-qualified] is neither a term of art nor a defined term for purposes of ERISA."); *In re Baker*, 114 F.3d at 638 (determining that the phrase "ERISA-qualified" merely addresses the question of "whether a creditor can reach the funds in bankruptcy"). See *supra* Part III.C regarding tax-qualification. The basic post-

more directly upon the question of how tax-qualification should affect retirement plan asset protection.²²⁶

The prevailing view today is that in using the term "ERISA-qualified," the *Shumate* Court was referring to retirement plan interests subject to the anti-alienation mandate set forth in § 206(d)(1) of the ERISA labor title without regard to whether the plan satisfied the tax-qualification criteria that include the ERISA tax title's I.R.C. § 401(a)(13) anti-alienation language. In this regard, Judge Easterbrook of the Seventh Circuit succinctly articulated both the question raised by *Shumate* and its more accepted resolution:

What is an 'ERISA-qualified' plan? The term does not appear in the statute, and its provenance is mysterious. Some plans are *tax-qualified*, a term of art meaning that contributions to the plan are deductible at the corporate level and not taxed to the employee until the plan distributes benefits. Taxation has nothing to do with the question at hand, however. Most likely, the Court used 'ERISA-qualified' to mean 'covered by Subchapter I of ERISA'. . . . Understanding 'ERISA-qualified' to mean nothing more complex than 'containing the anti-alienation clause required

Shumate split among the Bankruptcy Courts pertains to whether "ERISA-qualified" meant that a plan: (1) was subject to ERISA; (2) was tax-qualified per I.R.C. § 401(a); and (3) included an anti-alienation provision—or: (1) was subject to ERISA; (2) included an anti-alienation provision; and (3) this provision is enforceable under ERISA. See, e.g., *In re Bennett*, 185 B.R. 4, 6 (Bankr. E.D.N.Y. 1995) (discussing the split of opinion among Bankruptcy Courts over relevance of tax-qualification to *Shumate*'s articulation of an "ERISA-qualified" benchmark); see also Sabino & Clarke, *supra* note 35, at 615 (discussing the split of judicial opinion regarding the relevance of tax-qualification to protected status). See *infra* notes 225–227 and accompanying text for further examples of post-*Shumate* disagreements.

Simply equating tax qualification to coverage under that portion of the ERISA labor title which includes § 206(d)(1) presents problems. This is due to the fact that some "tax-qualified" retirement arrangements are not subject to § 206(d)(1) of the ERISA labor title, and some arrangements subject to § 206(d)(1) are not tax-qualified. See *supra* notes 103–08 and 123–28 regarding plans subject to the dual ERISA anti-alienation mandates and exceptions to these requirements. Interestingly, the *Shumate* court acknowledged that many arrangements would fall outside of the 11 U.S.C. § 541(c)(2) exclusion under the Court's decision, specifically referencing governmental plans and IRAs, but in doing so the court cited both § 206(d)(1) and the regulations under I.R.C. § 401(a)(13) without further clarifying the dilemma that would confound subsequent courts left to wrest with the import of the Court's pronouncement. *Patterson v. Shumate*, 504 U.S. 753, 762 (1992). Arrangements subject to neither § 206(d)(1) nor § 401(a)(13) would include, for example, an individual retirement arrangement held in the form of a qualified annuity, rather than a trust or custodial account arrangement falling within the scope of I.R.C. § 401(a)(13) (2000). See, e.g., *In re Fulton*, 240 B.R. 854, 862–68 (Bankr. W.D. Pa. 1999) (discussing this distinction).

226. Almost a decade later, this very concept is now driving congressional attention to this area. See *infra* Part IV.C (discussing proposed bankruptcy legislation grounded in the criteria of tax-qualification).

by § 206(d)(1) of ERISA' makes the phrase mesh with the topic of the opinion: [namely,] . . . whether a creditor can reach funds in bankruptcy.²²⁷

Thus, since *Shumate*, one can readily conceive The Federal Retirement Model as bifurcated between plan interests that are entitled to a blanket § 541(c)(2) exclusion under *Shumate*, and those that are not. The bulk of tax-qualified Keogh plans and IRAs are important arrangements on the exposed side of the post-*Shumate* bifurcation in retirement plan asset protection.²²⁸ These plans fall outside the scope of ERISA's § 206(d)(1) anti-alienation mandate and must therefore find asset protection through other avenues, if at all. The asset protection analysis applicable to these arrangements is multilayered and warrants further exploration.²²⁹

First, an anti-alienation provision derived from outside of ERISA might affect a plan that is not ERISA-qualified. So long as the anti-alienation provision is deemed enforceable under traditional spendthrift trust principles²³⁰ or some other governing statute,²³¹ an exclusion under § 541(c)(2) will protect

227. *In re Baker*, 114 F.3d at 638. This case was the first Circuit Court opinion to address the relevance of tax-qualification to a plan's status as "ERISA-qualified" within the meaning of *Shumate*. *In re Sewell*, 180 F.3d at 712.

The term "ERISA-qualified" will hereafter be used to denote plan interests subject under ERISA's labor title to the § 206(d)(1) spendthrift mandate, and the term "tax-qualified" will continue to be used in the distinct manner described in *supra* note 120.

228. A Keogh plan is not subject to ERISA where the plan does not include employees other than the business owner. Dep't of Labor Reg., 29 C.F.R. § 2510.3-3(b) (1975). However, if the plan does include non-owner employees then it will be covered under Title I of ERISA. *Id.* Similarly, IRAs are excluded from coverage under Title I. Dep't. of Labor Reg., 29 C.F.R. § 2510.3-2(d)(1) (1975). See *supra* note 123 and the discussion in *supra* Part IV.B regarding IRAs and Keogh plans and their coverage under ERISA. Unfunded deferred compensation arrangements would also fall outside the *Shumate* protection. With respect to unfunded and other NQDC arrangements, see *supra* note 130.

229. As to the importance of examining asset protection for these arrangements that fall outside the protection of *Shumate*, one need merely note that the sheer dollar amount held in IRAs exceeds the amounts held in either the more traditional employer-sponsored DB plans or the increasingly prevalent DC plans. See JCX-9-02, *supra* note 16, at 34 (reporting that as of December 31, 2000, IRAs held \$2.65 trillion, DC plans held \$2.53 trillion and DB plans held \$2.06 trillion).

230. Outside the context of pension plans covered by ERISA, *Shumate* left intact the well-established principle that non-ERISA trust interests otherwise protected under traditional state spendthrift trust law doctrines remained within the ambit of the 11 U.S.C. § 541(c)(2) exclusion. *Patterson v. Shumate*, 504 U.S. 753, 762 (1992) (noting that the legislative history of 11 U.S.C. § 541(c)(2) clearly indicates the congressional intent to continue the exclusion of spendthrift trust interests protected under applicable state law); see also *In re Wilcox*, 233 F.3d 899, 904 (6th Cir. 2001) (addressing this aspect of the *Shumate* decision).

231. Plans not subject to ERISA § 206(d)(1) might still find protection in the nature of an exclusion under § 541(c)(2) if an anti-alienation provision enforceable under federal or state law (other than ERISA) is present. This determination may hark back to pre-*Shumate* spendthrift

the interest. For many plans not "ERISA-qualified," therefore, the same traditional analysis underlying the reasoning of the dominant faction of the circuit courts prior to *Shumate* may determine whether the retirement plan is protected. For example, courts sometimes deem debtor interests in IRAs and Keogh plans as excluded from the bankruptcy estate post-*Shumate* by virtue of the interaction of state spendthrift trust law and § 541(c)(2), giving new life even to the I.R.C. § 401(a)(13) anti-alienation mandate that is *not* generally regarded as unilaterally enforceable.²³² As was the case for many plans prior to

trust analysis or may turn upon the implications of *Shumate*'s construction of the phraseology "enforceable under applicable nonbankruptcy law." *Shumate*, 504 U.S. at 758. For example, some post-*Shumate* debtors have found blanket protection similar to that accorded to ERISA-qualified plans by virtue of particularized statutes that impose enforceable anti-alienation limitations upon certain retirement arrangements—thus constituting restrictions that are "enforceable under applicable nonbankruptcy law." See, e.g., *In re Mueller*, 256 B.R. 445, 461 (Bankr. D. Md. 2000) ("Applicable nonbankruptcy law in the instant case is found in the Annotated Code of Maryland . . ."). Indeed, a post-*Shumate* circuit split has arisen as to whether such anti-alienation provisions must appear in the plan itself, or if the presence of an anti-alienation provision in external law is sufficient to bring an interest within 11 U.S.C. § 541(c)(2). See, e.g., *In re Wilcox*, 233 F.3d at 904 (holding that anti-alienation provision included in city charter was sufficiently enforceable to warrant exclusion under 11 U.S.C. § 541(c)(2) as construed by *Shumate*), cert. denied sub nom. Taunt v. Gen. Retirement Sys. of Detroit, 533 U.S. 929 (2001); *In re Lowenschuss*, 171 F.3d 673, 683 (9th Cir. 1999) (noting the creation of a circuit split by rejecting *Meehan* and *Yuhas* and holding that 11 U.S.C. § 541(c)(2) as construed by *Shumate* requires that the transfer restriction be contained in the trust instrument itself); *In re Yuhas*, 104 F.3d 612, 614–15 (3d Cir. 1997) (holding that a 1993 New Jersey statute which looks very much like an exemption statute imposes a restriction on the transfer of IRA holder's interest within *Shumate*, thus causing that interest to be excluded from the IRA holder's bankruptcy estate under § 541(c)(2)); *In re Meehan*, 102 F.3d 1209, 1210–11 (11th Cir. 1997) (concluding that Georgia exemption statute excludes debtor's IRA from bankruptcy estate despite the absence of an anti-alienation provision in the IRA documents); *In re Zott*, 225 B.R. 160, 163–64 (Bankr. E.D. Mich. 1998) (rejecting the *Meehan* analysis and concluding that the transfer restriction must be included in the trust itself and be enforceable for the exclusion under 11 U.S.C. § 541(c)(2) to pertain). For a decision excluding a debtor's interest in a retirement plan by virtue of some federal law other than ERISA, see *In re Whetzal*, 32 F.3d 1302, 1304–05 (8th Cir. 1994) (relying on *Shumate* in holding that a federal employee's right to lump-sum distribution under the Civil Service Retirement System was excluded from a bankruptcy estate by virtue of interaction of 11 U.S.C. § 541(c)(2) and 5 U.S.C. § 8346(a)). With regard to I.R.C. § 401(a)(13) constituting a separately enforceable anti-alienation provision, see *supra* notes 123–125 and *infra* note 232 and accompanying text.

232. See *In re Moses*, 167 F.3d 470, 472–74 (9th Cir. 1999) (holding that debtor-physician's interest in a Keogh plan was excluded under 11 U.S.C. § 541(c)(2) by virtue of the I.R.C. § 401(a)(13) anti-alienation provision and the plan's status as a spendthrift trust under California state spendthrift trust law, where the debtor did not control the plan or sponsoring physician practice group). The anti-alienation requirement for tax-qualification set forth in I.R.C. § 401(a)(13), however, is generally held to fall short of the unilaterally enforceable anti-alienation requirement implicated by § 541(c)(2) under the reasoning of *Shumate*. See also SPERO, *supra* note 212, § 10.04(1)(a) (noting cases on point and concluding that "[t]he I.R.C. provision merely relates to controversies arising in connection with the IRS determination that a

Shumate, however, these non-ERISA-qualified retirement plans often fail such a traditional analysis by virtue of both the self-settled nature of the arrangement and the liberality of the debtor-settlor's control over and access to the funds.²³³ The continued willingness of courts to look beyond the facial claim of spendthrift protection in order to determine whether asset protection is justified on retirement policy grounds further compounds the post-*Shumate* contrast in asset protection analysis.²³⁴

A second and final stop in the multi-layered quest for asset protection outside the confines of *Shumate* is the recognition that, in many instances, an exemption might shield a retirement plan interest from creditors.²³⁵ Once again, potential asset protection discrepancies arise. These discrepancies are attributable to the federal bankruptcy opt-out exemption scheme. Under that scheme, either state or federal law may define the exemption.²³⁶ Therefore, many variations exist with respect to both the extent of the exemptions and the

trust holding plan assets is entitled to tax-exempt status Consequently, an I.R.C.-mandated anti-alienation provision would not [in and of itself] constitute 'applicable nonbankruptcy law' for . . . purpose[s] of the § 541(c)(2) exclusion. "); 2 NORTON BANKRUPTCY LAW AND PRACTICE 2D § 156.5 (William L. Norton Jr. ed., 1997) ("However, since I.R.C. § 401(a), and, in particular, the anti-assignment/anti-alienation provisions of I.R.C. § 401(a)(13), do not appear to have independent substantive effect (unlike ERISA § 206(d)(1)), it is not clear why tax-qualification under I.R.C. § 401(a) should be relevant to a § 541(c)(2) exclusion."). Regarding I.R.C. § 401(a)(13), see also *supra* notes 123–25 and 231 and accompanying text.

233. Compare *In re Lowenschuss*, 171 F.3d at 680–83 (holding that a sole owner plan was subject to creditor claims as part of bankruptcy estate and specifically *rejecting* arguments that: (1) the plan was excludable as ERISA-qualified; (2) a provision in a state law constituted a restriction on transfer enforceable under applicable nonbankruptcy law; and (3) the debtor's interest in the plan was a valid spendthrift trust under state law—with the debtor's access to and control of the plan funds playing a significant role in rejection of this latter argument), with *In re Silveira*, 186 B.R. 168, 172 (Bankr. D. Mass. 1995) ("Thus, the element of control and access to the retirement funds which featured prominently in the analyses of the courts [prior to *Shumate*] is no longer determinative in situations where the applicable nonbankruptcy law is law other than state spendthrift trust law.").

234. See, e.g., *In re DeNadai*, 259 B.R. 801, 808 (Bankr. D. Mass. 2001) (refusing to exclude incentive savings arrangements by analogy to ERISA-qualified plans protected under *Shumate*, and noting that with regard to anti-alienation restrictions originally included in the arrangement, "there is no evidence that those restrictions were for trust purposes akin to the concerns surrounding, and protection of, retirement benefits").

235. The exemption analysis follows only where the interest fails the standards for excludability under 11 U.S.C. § 541(c)(2). See *supra* note 182 and accompanying text (discussing the use of exemptions for sheltering property in bankruptcy proceedings); see, e.g., *In re Lutge*, 204 B.R. 259, 263 (Bankr. S.D. Fla. 1997) (holding SEP/IRA arrangement exempt under Florida exemption statute).

236. The exemption opt-out scheme is discussed *supra* notes 183–85.

nature of the arrangements protected.²³⁷ For example, debtors subject to the federal exemption scheme must contend with language that exempts:

The debtor's right to receive . . . a payment under a stock bonus, pension, profit sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless . . . such plan or contract does not qualify under section 401(a), 403(a), 403(b) or 408 of the Internal Revenue Code²³⁸

Observers hoping to understand the post-*Shumate* variations in retirement plan asset protection must note three important differences between this exemption and the blanket protection afforded to an ERISA-qualified plan. First, through specification of "similar plan" and five circumstantial criteria (illness, length of service, etc.), the federal exemption statute protects only those interests that are sufficiently tied to retirement or similarly unavoidable needs.²³⁹ Second, the statute further limits the protection afforded a debtor's retirement plan interest to that which is "reasonably necessary for support."²⁴⁰

237. For a compilation of the protection afforded under the exemption laws of the various states, see 1997 FINAL REPORT, *supra* note 184, at 299; 1 DUNCAN E. OSBORNE & ELIZABETH MORGAN SCHURING, ASSET PROTECTION: DOMESTIC AND INTERNATIONAL LAW AND TACTICS §§ 10.08-10.58 (1997).

238. 11 U.S.C. § 522(d)(10)(E) (2000). See *Patterson v. Shumate*, 504 U.S. 753, 762 (1992) (rejecting the proposition that the presence of an exemption under 11 U.S.C. § 522(d)(10)(E) somehow implicated the absence of an available ERISA exclusion under 11 U.S.C. § 541(c)(2), precisely reasoning that the former provision was broader in scope and thus not rendered superfluous by the court's holding). Among the plans that might fall within 11 U.S.C. § 522(d)(10)(E) but that are clearly outside the scope of ERISA are plans maintained by governmental and church entities, IRAs, and certain plans covering only a sole owner but no nonowner employees. *Id.* at 762-63. For a case applying the California exemption statute, CAL. CIV. PROC. CODE § 703.140(b), which mirrors Bankruptcy Code § 522(d)(10)(E), see generally *In re McNown*, 203 F.3d 1188 (9th Cir. 2000).

239. Courts generally interpret the statutory language to require that the interest be in "pay status" or that the debtor be sufficiently close to retirement age that the debtor's ability to provide for present needs would be hindered by the urgent need to restore a creditor-depleted retirement fund. Some courts have held that only those benefits that a debtor has a present right to receive (i.e., in "pay status") are subject to exemption, although the better reasoned view focuses upon the debtor's immediate post-bankruptcy fresh start and the degree to which the lack of asset protection would hinder that fresh start in light of the (impending) immediacy of the retirement needs. See, e.g., *In re Fulton*, 240 B.R. 854, 875-76 (Bankr. W.D. Pa. 1999) (discussing contrary cases but resolving the issue by reference to retirement interest as impacting relatively short-term needs for a debtor who was age fifty-five at the time of bankruptcy filing). Thus, younger debtors are much less likely to avail themselves of any exemption under 11 U.S.C. § 522(d)(10)(E) because the need for retirement funds is not as urgent, and thus the courts are less likely to grant any exemption. *Id.* at 876.

240. See *In re Kramer*, 249 B.R. 147, 149 (Bankr. E.D. Mich. 2000) ("It is helpful to separate the analysis . . . into three issues: (1) whether the IRAs may be considered 'similar

Courts and commentators have construed this limitation in the retirement plan context to mean protection only for rights necessary to maintain a minimal (i.e., Social Security floor type) standard of living in the near term, consistent with the bankruptcy fresh start objective. This limitation is applied without regard to a debtor's future retirement income needs or any standard of living to which the debtor may have become accustomed.²⁴¹

plans or contracts'; (2) whether payments that may be triggered for reasons other than the five 'on account of' factors are protected; and (3) whether the payments are reasonably necessary for support.").

The reasonably necessary criteria implicates several lines of analysis mooted by *Shumate* in the context of an ERISA-qualified plan. For example, some courts have denied exemption to IRAs on the basis of a debtor's essentially unfettered withdrawal rights, although the prevailing trend seems to read the statute as favoring exemption for IRAs without regard to the debtor's control over the withdrawal decision. *In re Kramer*, 249 B.R. at 151. In reluctantly finding the exemption proper under the language of the statute, one court specifically noted that as applied to IRAs, "this exemption protects a right to payment from a revocable, self-settled trust." *Id.* The same court further questioned the degree to which IRAs truly serve any retirement objectives in light of the liberality of the applicable withdrawal rules. *Id.* The court cites, in its discussion, academic commentary raising similar concerns about the retirement orientation of IRAs. See Dilley, *supra* note 35, at 415–29 (examining the rationale for affording protection to IRAs in bankruptcy proceedings); Kaplan, *supra* note 136, at 303–09 (noting concerns regarding preretirement withdrawals from IRAs).

The more technical arguments levied against exempting IRAs generally were that the debtor's unilateral right to withdraw IRA funds prior to age 59½ and the absence of similar limitations meant that the IRA was either not similar to the enumerated types of plans or that payment was not limited to the specified events. There are four basic arguments that courts have offered in support of finding an exemption for IRAs: (1) Congress must have intended to include such plans as similar to those enumerated, or else the exception of only certain IRAs from exemption under 11 U.S.C. § 522(d)(10)(E)(iii) would make no sense; (2) IRAs are substitutes for future earnings because they were designed by Congress specifically to provide retirement benefits; (3) to deny exemption would penalize those individuals not eligible for an employer-sponsored retirement arrangement; and (4) the exemption is consistent with the bankruptcy fresh start given the "reasonably necessary" limitation. See *In re Brucher*, 243 F.3d 242, 243 (6th Cir. 2001) (noting the trustee's objections and summarizing the arguments in favor of exemption); *In re Carmichael*, 100 F.3d 375, 378–79 (5th Cir. 1996) (discussing the requirement that amounts be payable on account of the listed event criteria, but holding that the debtor's access to and control over funds, which implicates that payments may be made for reasons wholly unrelated to five stated events, does not disqualify IRA from exemption); *In re Kramer*, 249 B.R. at 150 (discussing judicial disagreement on the issue of whether the five enumerated events are an exclusive list of payment reasons, and reluctantly concluding that statutory language dictates that a right to payment for reasons other than the five enumerated events will not disqualify a plan for exemption, so long as a right to payment relating to the five events is present); *In re Hermes*, 239 B.R. 491, 495–97 (Bankr. E.D. Mich. 1999) (discussing the legislative history of 11 U.S.C. § 522(d)(10)(E) and the protection of benefits which are akin to future earnings, and also noting discrimination against the self-employed issue were the protection to be denied to certain interests).

241. See *In re Taff*, 10 B.R. 101, 107 (Bankr. D. Conn. 1981) (discussing the meaning of "reasonably necessary" in a case of first impression for bankruptcy courts, and concluding that

The presence of such a considered limitation outside the confines of an excluded ERISA-qualified plan presents a stark legislative contrast. Specifically, in developing the 1978 Code, the Senate attempted to impose a "reasonably necessary" limitation upon the § 541(c)(2) *exclusion* approach to protecting traditional spendthrift trusts.²⁴² Any excess above the amount necessary to satisfy this standard would have been subject to forced application in satisfaction of creditor claims.²⁴³ The full Congress rejected the Senate's

"the . . . amount to be set aside for the debtor ought to be sufficient to sustain basic needs, not related to his former status in society or the lifestyle to which he is accustomed"); *see also* Dilley, *supra* note 35, at 410 (noting that 11 U.S.C. § 522(d)(10)(E) is consistent with the idea of protecting only a minimal stream of income upon retirement). Regarding lifestyle maintenance as an aspect of the retirement income security goal, *see supra* notes 62–63, 75–77, and 84–87 and accompanying text.

242. *See* S. REP. NO. 95-989, at 83 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5869 (stating that the exclusion is limited to "income that is reasonably necessary for the support of a debtor and his dependents"). Of course, as noted *supra* Part IV.B.2, § 541(c)(2) ultimately became a direct means for protecting "ERISA-qualified" plans without regard to traditional spendthrift trust analysis.

243. Congress created a special commission in 1970 to assist with the impending bankruptcy reform that would ultimately culminate in the enactment of the 1978 Code. *See supra* note 185 (noting the creation of the Commission on Bankruptcy Laws). As part of its 1973 report, that Commission recommended to Congress that the spendthrift trust bankruptcy exclusion (now embodied in § 541(c)(2)) be limited so as to protect *only* that amount of trust property or interest necessary to provide for the reasonable support needs of the beneficiary and her dependents. *See supra* notes 172–93 and accompanying text (explaining the exclusion of spendthrift trust property under the prior 1898 Act). This recommendation is embodied in § 4-601(b) of the Commission's proposed statute included in the 1973 Commission Report, *supra* note 185, which was a focal point of debate concerning the impending new bankruptcy legislation. The Senate endorsed the Commission's opinion that:

There is no sound justification for permitting a debtor to take advantage of the [protections afforded under federal bankruptcy laws] and, at the same time, to shield from his creditors assets because local law does not allow creditors to reach his interest. The Commission generally recommends that these restraints not be enforceable. However, in recognition of the possibility that the spendthrift trust may be used to protect one incapable of providing for his own welfare, the debtor should be allowed to retain sufficient income to support himself and his dependents. But to the extent the beneficial interest is of a value in excess of the reasonable support needs of the debtor and his dependents, the interest should be available to the debtor's creditors.

1973 Commission Report, *supra* note 185, at 486. The notes to the Commission's proposed § 4-601 state that:

If the income exceeds such amount [as may be necessary to support the debtor and the debtor's dependents], the [bankruptcy] trustee can sell the right to the excess income, hold open the case so as to collect the income, or reach the principal to the extent in excess of the principal needed to generate the support income . . . subject, of course, to the rights of any third persons in the principal.

Id. For additional explanation of how a creditor might realize upon a beneficial interest such as

view, however, and enacted § 541(c)(2) without limit upon the amount sheltered.²⁴⁴

The legislative history of the *exemption* granted under the 1978 Code § 522(d)(10)(E) is just the opposite. Both the Senate and House proposed exemption provisions that conferred asset protection upon affected retirement plans *without* any needs-based or other dollar limitation.²⁴⁵ Through the reconciliation process, however, legislators *added* the "reasonably necessary" limitation to the final version of § 522(d)(10)(E).²⁴⁶ Congress therefore consciously rejected any "reasonably necessary" cap on the amount to be protected from creditors under an *exclusion* that clearly embraced the wealth-driven traditional spendthrift trust under state law.²⁴⁷ In contrast, retirement plan interests emerged with: (1) uncertain and seemingly little considered coverage under this broad § 541(c)(2) exclusion, as evidenced by *Shumate* and the antecedent circuit split;²⁴⁸ and (2) a federal exemption provision capped by an asset protection limiting "reasonably necessary" standard under § 522(d)(10)(E). It is, therefore, hardly surprising that the proper scope of retirement plan asset protection has proven so elusive.

The third difference between protection by exemption and protection under *Shumate* is the degree of inconsistency that arises when similarly situated debtors attempt to exempt retirement plan interests. For interests that fall

that held by a trust or retirement plan beneficiary, see *supra* note 21.

244. H.R. REP. NO. 95-595, at 367-69 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6323-6325. See 124 CONG. REC. H11,096 (daily ed. Sept. 28, 1978) (remarks of Rep. Edwards) (discussing limitations on § 541(c)(2)); 124 CONG. REC. S17,413 (daily ed. Oct. 6, 1978) (remarks of Rep. Edwards and Sen. DeConcini) (same). The legislative history of the completed 1978 Code contains no meaningful discussion of the issue.

245. See H.R. REP. NO. 95-595, at 361 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6317 (proposing bankruptcy legislation that allowed retirement plans to be protected from creditors in bankruptcy without need-based limitations). The bill reported out of the Senate judiciary committee actually deferred the entire matter to states, without federal limitation on states' ability to exempt these interests. See *In re Taff*, 10 B.R. at 106 (discussing the Senate proposal regarding exemptions in the context of § 522(d)(10)(E)).

246. Congress provided no explanation as to how that standard might be applied. For a thorough discussion of the legislative history of 11 U.S.C. § 522(d)(10)(E) and the co-existing limitation under the Uniform Exemptions Act as promulgated in 1976, see the court's discussion in *In re Taff*, 10 B.R. at 105-06. The *Taff* court concluded that Congress omitted any guidance on the question of the "reasonably necessary limitation . . . because it expected the courts to evolve standards on a case-by-case basis." *Id.* at 106. For criticism of this case-by-case approach, see *infra* notes 331-33 and accompanying text.

247. Regarding references in the legislative history of § 541(c)(2) to protection for state law denominated spendthrift trusts, see *supra* notes 202-05 and the accompanying text.

248. See *supra* Part IV.B.1 and accompanying text (discussing judicial interpretation of ERISA's impact on asset protection in bankruptcy).

outside the scope of *Shumate*, Congress has elevated federalism concerns over national retirement policies by expressly permitting states to opt-out of the federal exemption scheme of which § 522(d)(10)(E) is a part.²⁴⁹ While some opt-out states have statutes that echo the language of the federal exemption, many do not.²⁵⁰ Instead, some state exemption statutes grant unlimited protection to "retirement" arrangements that are delineated by reference to the various tax-qualification rules of the I.R.C.²⁵¹ The arrangements so defined typically include IRAs and other arrangements not "ERISA-qualified"—and thus not otherwise entitled to such sweeping protection under any federal law.²⁵²

Some have criticized the amorphous state of retirement plan asset protection on the grounds that inconsistency in treatment of retirement plan types leads to inequities as between persons eligible to participate in (and to receive *Shumate* asset protection under) an ERISA-qualified plan, and those ineligible for such coverage by virtue of, for example, their status as self-employed.²⁵³ Forcing IRAs and Keogh plans to fit within the sometimes limited protective parameters of an exemption is not necessarily inconsistent with ERISA's overriding purpose, however, given the individual participant's control over funding and management of such plans and the absence of employees generally.²⁵⁴ On the other hand, this discrepancy is a somewhat odd result given that IRAs originated under ERISA as an alternative for such ineligible individuals, and also in light of the I.R.C. provisions that equate the funding of a Keogh plan to that of an employer-sponsored plan.²⁵⁵

249. As noted, approximately thirty-five states have opted-out of the federal exemption scheme. See *supra* note 185 and accompanying text (describing the limitations imposed on debtors in opt-out states with regard to exemptions).

250. For an example of a state statute that mirrors the federal exemption, see CAL. CIV. PROC. CODE § 703.140(b), as discussed in *In re McKown*, 203 F.3d 1188, 1189 (9th Cir. 2000).

251. Like the *Shumate* Court's imprecise use of the phrase "ERISA-qualified," this is but another asset protection standard of varying applicability that highlights the question of what role retirement plan tax-qualification should play in retirement plan asset protection analysis.

252. IRA exemption under 1978 Code § 522(d)(10)(E) is subject to a "reasonably necessary" limitation.

253. See, e.g., *In re Hermes*, 239 B.R. 491, 496 (E.D. Mich. 1999) ("Failure to treat IRAs as 'similar plans' and thus exempt [under 11 U.S.C. § 522(d)(10)(E)] would be to penalize individuals who are not in a position to participate in a pension plan or profit sharing plan, e.g., self-employed individuals.").

254. See, e.g., *In re Lowenschuss*, 171 F.3d 673, 681 (9th Cir. 1999) (noting that no ERISA protection is called for where the sole plan participant also is the plan administrator).

255. See *supra* note 123 and *supra* Part IV.B regarding IRAs and Keogh plans and their coverage under ERISA. See also MUNNELL, *supra* note 28, at 55 ("In passing ERISA, Congress recognized that a large segment of the working population was ineligible for the tax advantages associated with private pension plans. Therefore, ERISA established individual retirement

In sum, asset protection within the Federal Retirement Model is now bifurcated between retirement plan interests that are unilaterally protected under *Shumate* and those that are not. Particular points of departure are: (1) the unquestioning asset protection available to ERISA-qualified and other statutorily enforceable spendthrifted arrangements by virtue of the § 541(c)(2) exclusion;²⁵⁶ versus (2) a myriad of sometimes inconsistent protection offered to non-ERISA-qualified arrangements through traditional state law spendthrift trust analysis;²⁵⁷ versus (3) broadly applicable but more demanding exemption laws that refer to tax-qualification, reasonable necessity, or distance from retirement as important criteria for protection;²⁵⁸ versus (4) state exemption laws that offer blanket protection based solely upon a retirement plan's tax-qualified status, without regard to the amount of assets protected or the real likelihood of actual retirement use.²⁵⁹ Given the prominence of federal retirement policy goals,²⁶⁰ it is counterintuitive that a federal scheme would permit variations in state law to provide for some (but not all) debtors substantial retirement plan asset protection equivalent to that accorded ERISA-qualified plans. Federalism is no answer because the federal goal of retirement income security is affected by creditor access to retirement plan interests, and that goal does not vary by state.²⁶¹

Yet, Congress has endorsed a very complex system of retirement plan designs. That system has developed into an arena peppered with a myriad of approaches to both the degree of asset protection and the extent of policy-based analysis undertaken in defining that protection. The reasons, apart from federalism concerns, that such a system endures arguably lie in divergent perspectives on the propriety of asset protection, coupled with a general congressional failure to consider the broader asset protection landscape in any

accounts and liberalized contribution limits on Keogh plans for the self-employed.").

256. See *supra* notes 217–29 and accompanying text (discussing protection of ERISA-qualified plans under the 11 U.S.C. § 541(c)(2) exclusion).

257. See *supra* notes 230–34 and accompanying text (discussing debtor protection from creditors during bankruptcy for non-ERISA trusts interests).

258. See *supra* notes 235–48 and accompanying text (noting the protection afforded by statutory exemptions).

259. See *supra* Part IV.A.2 regarding the "opt-out" bankruptcy exemption scheme, and *supra* notes 249–51 and accompanying text regarding state exemption laws that do not impose a "reasonably necessary" limit on the protection of retirement plan interests.

260. See *supra* notes 221–22 (discussing the legislative objectives and social policies behind federal retirement law).

261. The tie between certain tax-qualified retirement plan interests and actual service to retirement policy goals is a topic developed more thoroughly in Part V.

focused or comprehensive manner.²⁶² More practically, however, the judicially perceived supremacy of ERISA doctrine where certain plan types are involved and the lack of clear guidance otherwise are perhaps the best explanations for the state of the law post-*Shumate*.²⁶³ Ultimately, a reasonable *Shumate* corollary appears to be that outside the context of an ERISA-qualified plan entitled to blanket exclusion under § 541(c)(2), Congress has made no firm (or at least consistently discernable) policy judgment about the proper boundaries of asset protection. Congress has therefore deferred the question of asset protection outside the confines of *Shumate* to the courts and/or states for resolution by reference to the same spendthrift trust, bankruptcy, tax, federalism, and retirement policy concerns that dominated the larger retirement plan asset protection landscape prior to *Shumate*. It now appears, however, that Congress has undertaken a fresh legislative approach to these issues.

C. A Third Legislative Progression in the Evolution of Retirement Plan Protection

Recent congressional attention to the matter of retirement plan asset protection indicates that a more expansive congressional policy judgment than that perceived by the *Shumate* Court is in the works.²⁶⁴ This judgment promises a shift towards a wider array of retirement-oriented directives serving as the basis for more broadly applicable asset protection. Specifically, proposed revisions to the 1978 Code (the Bankruptcy Amendments) have made several recent forays through Congress and presage what should be characterized as the third significant progression in the evolution of asset protection under the Federal Retirement Model.²⁶⁵ It appears that Congress too

262. The assertion that the asset protection variations are coherently tied to differences in plan type breaks down through simple reference to the variations in the treatment afforded similarly situated retiree-debtors, as discussed in the text accompanying *supra* notes 249–55, and also is undermined by the circuit splits that have arisen in the post-*Shumate* era, as discussed, for example, *supra* note 225.

263. Regarding the *Shumate* Court's conclusion that Congress deemed ERISA policy to trump creditor rights concerns, see *supra* notes 221–22 and accompanying text.

264. Regarding the *Shumate* Court's perception of congressional policy, see *supra* notes 221–22.

265. See Bankruptcy Abuse Prevention and Consumer Protection Act of 2001, H.R. 333, 107th Cong. (proposing numerous revisions to the Bankruptcy Code of 1978). The House of Representatives passed this Act by a vote of 306 to 108. 147 Cong. Rec. H600–01 (daily ed. March 1, 2001). A modified version of the House Bill passed the Senate by a vote of 82 to 16, and was denominated simply the "Bankruptcy Reform Act of 2001." H.R. 333, 107th Cong. (2001) (as amended by S. Amend. 974 and S. Amend. 977). Despite conference agreements in August 2002 and November 2002 on all other significant outstanding issues, a combination of

has noted the variable state of retirement plan asset protection in the post-*Shumate* world.²⁶⁶ Congress now proposes to streamline the analysis by simple reference to the general categories by which the "carrot" of tax incentives is bestowed.²⁶⁷

Under the Bankruptcy Amendments, significant asset protection expressly grounded in the criteria of tax-qualification finally rises to the forefront in marking the bounds of asset protection under the Federal Retirement Model. As to the proper balancing of bankruptcy versus retirement policies, the Bankruptcy Amendments facially reflect a congressional consensus that the tax-qualification rules are a sufficient delineation of means by which important federal retirement objectives are carried out.²⁶⁸ The Bankruptcy Amendments at the very least reflect a determination that the tax-qualification rules provide a reasonable benchmark by reference to which more consistent asset protection treatment can be accorded to the retirement plan types that are encouraged under federal tax laws.²⁶⁹ Moreover, on first impression, the closer tying of

postelection partisan politics and an ideological battle over the protection to be afforded abortion protestors in bankruptcy has most recently stalled the legislation. Links to the history of the Bankruptcy Amendments and the latest on the status of this legislation are available at <http://thomas.loc.gov/cgi-bin/bdquery/z?d107:HR00333:@@X> (last visited Nov. 9, 2003) (on file with the Washington and Lee Law Review). The legislation has shown remarkable resiliency, having remained afloat despite two Clinton vetoes and significant delays in conference action occasioned by the events of September 11, 2001. See 147 Cong. Rec. H517-18 (daily ed. March 1, 2001) (detailing the history of the legislation that preceded the currently pending Bankruptcy Amendments, and noting Clinton vetoes); see also Sheila Creaton, *Pro-Creditor Bankruptcy Reform Moves Quickly Through Congress*, LAWYERS WEEKLY USA, Feb. 19, 2001, at 1 (discussing a proposed bankruptcy bill and its provisions); Reni Gertner, *Bankruptcy, HMO Reform Are Stalled After Terrorists Attacks*, LAWYERS WEEKLY USA, Oct. 15, 2001, at 1 (noting delays in the passage of bankruptcy legislation following the September 11, 2001 terrorist attacks). The latest incarnation of this legislation now enjoys the support of President George W. Bush, who has indicated he will sign the new law if presented to him. *Id.* at 1.

266. The Bankruptcy Amendments actually have roots in legislation originally offered in response to the circuit split that preceded *Shumate*—perhaps forestalled by that decision but resurfacing of late due to more attentive congressional scrutiny of the continuing discrepancies in retirement plan asset protection, notwithstanding the *Shumate* "resolution" of such matters. See H.R. 3804, 102d Cong. § 2 (1991) (proposing to amend federal bankruptcy law to exclude from a debtor's estate any interest in certain qualified pension plans); S. 1985, 102d Cong. § 202 (1991) (proposing to establish a commission to review the Bankruptcy Code); JCS-16-91, *supra* note 35, at 6-8, 14 (discussing the pre-*Shumate* circuit split and the proposed house bill aimed at addressing the retirement plan asset protection issue responsible for that split).

267. See Part III.C regarding the tax-incentives and the categories of plans for which these benefits are available.

268. See *infra* note 271 and accompanying text (using that qualification as a criteria in determining what types of retirement plans fall under the federal exemption).

269. For example, references in the Senate debate point to the "equal protection" of various

asset protection to objective tax-qualification criteria seems to be a logical course to pursue if uniformity and simplicity are among the goals of this revisitation. In other words, when juxtaposed against the current backdrop of various federally sanctioned but non-federally derived controls over retirement plan asset protection, the increased uniformity in asset protection across plan types and debtors is one of the more defensible aspects of this congressional push towards tax-based asset protection.²⁷⁰

More technically, the Bankruptcy Amendments expressly adopt tax-qualification as the determinant of asset protection for a range of plans much broader than those within the ambit of ERISA § 206(d)(1) and *Shumate*. A preemptive federal exemption framework provides the new avenue for protection. That protection extends specifically to:

Retirement funds to the extent that these funds are held in a fund or account that is exempt from taxation under section 401 [profit sharing and stock bonus plans, including those of self-employed individuals], 403 [annuity plans, including those of certain tax-exempt organizations and educational organizations], 408 [individual retirement accounts, 408A [Roth IRAs], 414 [multi-employer plans], 457 [certain governmental plans], or 501(a) [tax-exempt trusts in which the bulk of tax-qualified plan assets are held] of the Internal Revenue Code²⁷¹

types of retirement plans that will result under a tax-based delineation of protected accounts. See, e.g., 147 Cong. Rec. S1925 (daily ed. March 7, 2001) (Statement of Sen. Hatch (R-Utah)) (referencing this argument). The Bankruptcy Amendments also are consistent with the findings of the 1997 Commission Report, which acknowledges the broad scope of protection afforded under *Shumate* and then concludes that protection for other retirement plans should be tied to tax-qualification criteria without the imposition of an extraneous "reasonable needs" standard, which the Commission felt fostered litigation due to its subjectivity. 1997 FINAL REPORT, *supra* note 184, at 139–41.

270. See, however, the discussion of shortcomings in the present retirement plan system, as noted *supra* notes 253–55 and accompanying text.

271. Bankruptcy Amendments § 224(a)(1), amending 1978 Code 11 U.S.C. § 522(b) (2000). More generally, § 224 amends and renumbers 1978 Code § 522(b) (as in effect on February 11, 2003) by adding a new § 522(b)(1), and then essentially renumbering the prior subsection (b) provisions. The new § 522(b)(1) expresses the authorization for exempting property in accordance with the newly numbered §§ 522(b)(2) and (b)(3). Renumbered § 522(b)(2), in turn, now embodies the applicability of federal exemptions under § 522(d), unless the debtor resides in an opt-out state. See *supra* notes 183–85 regarding the exemption opt-out scheme. If the debtor is proceeding under the § 522(d) federal list of exemptions, the language quoted in the text *supra* will govern by virtue of a new § 522(d)(12), as added by Bankruptcy Amendments § 224(a)(2). Newly numbered § 522(b)(3) embodies the opt-out exemption scheme, and where applicable the governing exemptions will be those provided under state law plus federal exemptions other than those set forth in § 522(d). In that case, however, the language quoted in the text *supra* still applies, now by virtue of newly added § 522(b)(3)(C)—in other words, federal law controls absolutely with respect to exemptions for the noted plans, regardless of the debtor's residence in an opt-out exemption state. Thus,

This language relegates to the annals of history many of the analytical considerations affecting the availability of asset protection both before and after *Shumate*. For example, the new legislation omits any caveat for debtor access or control, and it does not inquire into the likelihood that retirement uses will actually ensue.²⁷² The legislation eliminates distinctions between trust and other plan forms, and the broad language likewise moots the issue of self-settlement.²⁷³ Debtors' interests in IRAs, Keogh plans, and other arrangements previously omitted from the § 541(c)(2) exclusion approach under *Shumate* will now enjoy *Shumate*-like protection in a federal bankruptcy proceeding. Further, this protection will not defer to variations in state exemption laws that might result in inconsistencies between otherwise similarly situated debtors.²⁷⁴ Also significant is the seeming relegation of "reasonable needs" exemption limits to retirement arrangements that fall outside the scope of either *Shumate* or this new tax-centric protection regime.²⁷⁵ But, some vestige of limitation

language substantially identical to that quoted in the text *supra* will govern a debtor proceeding under the federal exemption scheme by virtue of amended § 522(b)(2) and newly added § 522(d)(12), and will govern a debtor opting out of the federal scheme by virtue of newly added § 522(b)(3)(C). In either event, the quoted language applies without regard to the "reasonably necessary" limitation in current § 522(d)(10)(E), and thus protection for the affected interests would seem to be beyond limitation under that standard. However, an absolute dollar ceiling limitation does apply to a debtor's interest in an IRA, as discussed *infra* note 276 and accompanying text.

272. See *supra* notes 212–34 and the accompanying text regarding the relevance of debtor access and control in resolving retirement plan asset protection questions.

273. See *supra* Part III.B.3 regarding plan forms and asset protection under ERISA. See *supra* notes 212–13 and accompanying text for discussion of self-settlement.

274. See *supra* note 270 (noting inconsistencies in treatment of similarly situated debtors under various state exemption statutes). In any federal bankruptcy proceeding, the specified exemptions under the Bankruptcy Amendments should preempt any divergent state exemption laws relating to the affected retirement arrangements notwithstanding retention of the opt-out scheme, as the new exemptions are provided for regardless of the applicability of federal versus state law exemptions. In this sense, the new provisions are a limitation on a state's ability to opt out of the federal scheme. However, state law exemptions would continue to be relevant in a state law insolvency proceeding. See Peter Spero, *Impact of Bankruptcy Reform Legislation on Asset Protection*, 28 EST. PLAN. 291, 295 (2001) (discussing the importance of state exemptions).

275. However, nothing indicates that more generous state law exemptions have been precluded for this more narrow category of arrangements. For example, a debtor's interest in a so-called "top hat" plan would be left to 11 U.S.C. § 522(d)(10)(E) or a state exemption scheme. A top hat plan generally is an unfunded arrangement designed to provide deferred compensation to a select group of highly compensated employees, and such arrangements are excluded from coverage under Title I of ERISA and also are not tax-qualified. Included within the rubric of top hat plans are phantom stock arrangements and SERPs. Also outside the scope of the Bankruptcy Amendments and *Shumate* protections would be any excess benefit plan—meaning a plan which exists primarily to provide benefits to employees which exceed the limitations on contributions and benefits specified in I.R.C. § 415. See ERISA, Pub. L. No. 93-406, 88 Stat.

does remain. For example, Congress singled out standard and Roth IRAs for special treatment, which comes in the form of an inflation-adjusted \$1,000,000 cap on the aggregate account balance to be shielded from creditors.²⁷⁶

D. In Search of Perspective

The noted progressions in the evolution of retirement plan asset protection continue to raise many questions, not the least of which is the logic of subjecting such a pervasive federal policy—retirement income security for citizens—to the vagaries of the currently bifurcated Federal Retirement Model of asset protection. The proposed legislative solution, which calls for an

829, § 3(36) (codified as amended in 29 U.S.C. § 1002(36) (2000)) (defining "excess benefit plan"); ERISA § 4(b)(5) (exempting unfunded excess benefit plans from the scope of Subchapter I of Title I of ERISA); 29 U.S.C. § 1003(b)(5) (same).

276. Bankruptcy Amendments § 224(e), amending 1978 Code § 522(n). For a more evaluative commentary on this exemption cap, see *infra* notes 288–92 and accompanying text. The cited provision specifies that the \$1,000,000 amount "may be increased if the interests of justice so require." Bankruptcy Amendments § 224(e)(1). Amounts rolled over from an otherwise fully protected tax-qualified arrangement do not count against this cap. See *supra* note 141 regarding rollovers. These rolled-over amounts therefore retain their creditor-protected status notwithstanding the cap and without detracting from the limited IRA amount the debtor might otherwise shelter. Bankruptcy Amendments § 224(a)(4), amending 1978 Code § 522(b)(3)(C) & (D), § 522(n). Other changes caused by the Bankruptcy Amendments and not discussed above include provisions clarifying the extent of judicial inquiry into the status of a particular plan as tax-qualified. See Bankruptcy Amendments § 224(a)(1), amending 1978 Code 11 U.S.C. § 522(b)(4), as well as provisions exempting many plan interests from consideration as disposable income in a Chapter 13 proceeding. See generally Spero, *supra* note 274, at 294 (discussing Chapter 13 provisions).

In a surprising move given the exemption approach adopted for other arrangements, Congress excluded IRAs and I.R.C. § 529 tax-favored plans established to further educational (as opposed to retirement savings) pursuits from the bankruptcy estate by virtue of an amendment to § 541 of the 1978 Code. Bankruptcy Amendments § 225(a), amending the 1978 Code by adding a new 11 U.S.C. § 541(b)(5), (6). Even more surprising are the lengths to which Congress went to impose anti-abuse limitations upon this particular exclusion, such that the protection is limited only to those education plans: (1) created for certain lineal descendants of the debtor; (2) to the extent contributions were not in excess of statutory limitations; and (3) with respect only to funds deposited into such a plan more than two years prior to the bankruptcy filing, or up to \$5,000 with respect to funds deposited between one and two years prior to filing. *Id.* The inclusion of such "an elaborate statutory mechanism" to curtail abuse in the case of educational arrangements relative to the absence of such limitations in the context of more traditional arrangements prompted one asset protection author to quip that "Congress apparently . . . found abusive the prospect of debtors providing for their children's education." Spero, *supra* note 274, at 291. The distinction, however, most likely lies in some perceived preeminence of retirement-oriented vehicles as sanctioned under the I.R.C., with a more questioning grant of asset protection where a worthy but nonretirement goal is the subject of the tax incentive. See, in that regard, the analysis set forth *infra* Part V.

increased emphasis upon tax-qualification as the relevant criteria for otherwise virtually unquestioned protection from creditor claims, also demands attention. The ultimate issues concern both the justification for, and the proper scope of, asset protection to be afforded a debtor's retirement plan interest. Part V presents a concluding perspective on the matter of retirement plan asset protection and the interactions between the Traditional, Self-Settled, and Federal Retirement Models that have affected that issue. The interplay between the three models in light of the particular policy choices that Congress appears to have made (or consciously overlooked) along the way indicate that Congress should now adopt a more comprehensive and focused federal approach to asset protection. In particular, considering not only the theoretical but also the pragmatic underpinnings of the Federal Retirement Model, Congress should more thoughtfully consider the concept of asset protection as it affects national retirement policy.

V. Asset Protection Through The Lens of Federal Retirement Policy

A view of the modern asset protection environment reveals a Traditional Model long blessed at the federal level. That blessing includes the promise of deference, under federal bankruptcy laws, to state decisions concerning the parameters and acceptability of protecting property conveyed in trust for the benefit of a third-party. Likewise, the domestic emergence of the Self-Settled Model and the inconsistencies resulting from the opt-out bankruptcy exemption scheme have helped to inspire a burgeoning asset protection environment.²⁷⁷ Couple this with the scheduled congressional repeal of federal wealth transfer taxes,²⁷⁸ and it seems that the privilege of accumulating wealth to be enjoyed currently and then passed on to subsequent generations without depletion by the claims of outsiders has never been more vibrant than today, and that federal policy either encourages or passively favors such a state of affairs.

Yet, against this backdrop, commentators have criticized the congressional push to more closely associate the Federal Retirement Model's asset protection with tax-qualification. Commentators have focused particular criticism on the characterization of many of the affected arrangements as operating more like

277. The federal influences upon the development of the Traditional and Self-Settled Models, and the particular role played by the opt-out exemption scheme under federal bankruptcy laws, are discussed in detail in Eason, *supra* note 174, at 52–69.

278. Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 501; I.R.C. §§ 2210, 2264 (2000).

personal savings accounts than retirement vehicles.²⁷⁹ The problem is the potential for substantial wealth accumulation within the tax-qualified retirement plan environment, unrelated to actual retirement or other beneficiary-specific or societally meritorious objectives.²⁸⁰ The foregoing juxtaposition of asset protection models is not intended, however, to suggest that such criticism is unfounded, as the noted criticism on these points with respect to the Federal Retirement Model is coherently articulated and adequately defended.²⁸¹ Instead, these considerations suggest two distinct lines of analysis that bring this Article to conclusion. The first examines the broader implications of using the existing tax-qualified retirement plan regime as a benchmark for establishing asset protection boundaries. The second suggests the need for a more comprehensive view of the interrelationship between the Traditional, Self-Settled, and Federal Retirement Models as affecting federal retirement policy objectives.

A. Asset Protection with Feigned Purpose?

Consideration of the Traditional, Self-Settled, and Federal Retirement Models suggests that it is not asset protection or even self-settlement per se that has engendered such criticism of the movement to link retirement plan asset

279. See, e.g., Dilley, *supra* note 35, at 415–16 (arguing for a more inquiring grant of asset protection for "retirement" arrangements, and lamenting in this regard, "[t]he continuing transformation of the private pension system into employer-sponsored tax-favored savings arrangements (such as 401(k) plans), whose accumulations can be easily transferred to IRAs"); Spitzer, *supra* note 35, at 1296 ("A terrible inequity would be created if debtors were able to shield their funds from creditors . . . then turn around and withdraw those same funds for their own benefit . . ."). An early characterization of retirement arrangements as constituting tax-advantaged savings vehicles, at least in part, appears in Wohl, *supra* note 35, at 34. Wohl suggests asset protection for that portion of a retirement arrangement that can be attributed to asset accumulation for the purpose of meeting reasonable needs upon retirement, while denying protection for the savings portion of the arrangement. *Id.* Although suggesting that actuarial theory might play a role, Wohl generally defers on the question of what level of assets might be protected in the name of ensuring that "reasonable retirement needs" will ultimately be met. *Id.* at 34–35.

280. See, e.g., *In re Dudley*, 249 F.3d 1170, 1176–77 (9th Cir. 2001) (considering whether an IRA from which \$107,000 had been withdrawn to pay current living expenses could qualify for an exemption by virtue of similarity to a retirement plan under a state exemption that mirrored 11 U.S.C. § 522(d)(10)(E)); Dilley, *supra* note 35, at 363–64 ("I suggest that a larger problem is the blanket protection of tax-favored retirement accounts . . . which allows unlimited accumulation of funds without regard to whether those funds will actually be used for retirement or will even be necessary for the debtor's support in old age.").

281. See *supra* note 35 (noting the academic commentary on post-ERISA changes in retirement plan asset protection).

protection to tax-qualified status. Rather, objection lies more fundamentally in the prospect of asset protection that is unbounded by any principled purpose, and, in particular, protection that is unbounded by the often elusive purpose of serving federal retirement objectives in a focused and equitable way. The problems with the current movement towards using tax-qualification as the standard for retirement plan asset protection, therefore, do not stem from the elevation of federal retirement policy objectives over bankruptcy considerations or some other balancing failure in that regard.²⁸² The problems instead stem from the defensibility of the tax-qualification criteria as truly serving meritorious federal policy objectives in an equitable and efficient manner—such that protection gauged by reference to tax-qualification is warranted. In this view, then, criticism of asset protection in the retirement plan arena is better directed at the nature of the interests protected as truly serving the underlying federal goal of promoting the retirement income security of citizens. If such criticism endures in the face of linkage to tax-qualified status, then the broader view suggests that a more logical response lies in re-examining the relationship between the tax-qualification criteria and the federal policy objectives that are said to justify the underlying retirement plan tax expenditure.²⁸³ Given retirement policy's place atop the tax expenditure list²⁸⁴ and the trail of congressional and Supreme Court pronouncements as to the apparent superiority of retirement policy in the face of creditor claims,²⁸⁵ identifying the problem in the foregoing manner is, pragmatically speaking, the more useful line of inquiry.

B. Tax-Qualification as Promoting Retirement Policy Objectives

Tax-qualification criteria often have little to do with ensuring that the affected assets will actually be directed towards the retirement income security goals that serve as the underlying justification for both the tax expenditure and

282. See *supra* notes 221–22 regarding the Supreme Court's view of this balance.

283. The tax expenditure concept is discussed in more detail *supra* notes 150–58 and accompanying text. Part V will show the suggested examination to be more productive than efforts to disassociate asset protection from tax-qualification standards, or attempts to graft some extraneous near-term "reasonable needs" or other limitation upon the asset protection so afforded. Regarding practical issues attendant a debtor-specific "reasonable needs" approach, see *infra* notes 328–33.

284. See *supra* note 152 and accompanying text (discussing the favorable tax treatment for retirement plans and its impact on tax revenues).

285. See *supra* notes 221–22 and accompanying text (noting legislative and Supreme Court discussions of policies and objectives favoring retirement plan asset protection).

asset protection. A particular problem is that of "leakage," which denotes the diversion of retirement plan assets to nonretirement consumptive uses, like buying a house or enhancing near-term standard of living.²⁸⁶ The tax-qualification rules often foster leakage by permitting liberal withdrawal of plan assets in the form of lump-sum distributions or roll-overs from traditional pension plans to less restrictive arrangements like IRAs.²⁸⁷ Among other things, then, restricting this leakage would appear to be central to accomplishing overriding retirement income security objectives. Permitting creditors to seize retirement plan interests or assets suggests a form of leakage, and asset protection can therefore align with the broader goal.

If Congress constrained the tax-qualified plan regime to minimize leakage, then asset protection linked to that regime would be much less objectionable.²⁸⁸ Interestingly, the \$1,000,000 cap placed on the protection afforded IRAs under the Bankruptcy Amendments at least evinces recognition of the issue and poses an asset protection compromise that is perhaps reasonable in degree and practical in its implementation.²⁸⁹ But arguably, Congress should have included Keogh plans and similar participant-controlled arrangements that exclude non-owner employees in a more comprehensive dollar-capped category of protected arrangements. Doing so would have delineated a distinction between retirement-directed arrangements and mere tax-favored "retirement" savings plans that are easily diverted to personal consumption. A predetermined dollar cap so applied—viewed in tandem with the rationale underlying the tax-favored status afforded Keogh plans and IRAs—would better address the conceptual concern that protection for these plans is questionable in purpose, different from that underlying the Self-Settled Model.²⁹⁰ Leaving the more limited universe of plans that are not tax-qualified to the "reasonable needs" inquiry posed under the federal § 522(d)(10)(E) exemption, then, would

286. See Stein & Dilley, *supra* note 151, at 1402–07 (identifying three primary sources of leakage: (1) preretirement leakage, which denotes consumption of retirement assets prior to retirement; (2) premature exhaustion of benefits during retirement; and (3) failure to exhaust benefits for use during retirement, thus converting retirement assets to inheritable assets for consumption by descendants or other devisees). See generally 21ST CENTURY, *supra* note 57, at 20–21 (discussing the problem of leakage and providing statistics).

287. See *supra* notes 48, 216 (discussing federal laws that regulate distributions from retirement plans).

288. For a discussion of potential mitigation of the leakage problem and the difficulty associated with redressing the problem, see Stein & Dilley, *supra* note 151, at 1413–19.

289. See *supra* note 276 and accompanying text (explaining that standard and Roth IRAs are singled out for special treatment through an inflation-adjusted \$1,000,000 cap).

290. See *infra* notes 135–41 and accompanying text regarding the rationale underlying the original legislative authorization for IRAs and Keogh plans as an employer-sponsored plan alternative.

seemingly help round out the Federal Retirement Model with a semblance of limitation. Moreover, by proceeding along these lines, Congress could confine the inefficiency inherent in a global case-by-case "reasonable needs" standard to a smaller class of debtors acting outside the tax-qualified plan regime.²⁹¹ But, true limitation here would require foreclosing the possibility of more generous state exemptions for these arrangements, which currently thrive under the federal bankruptcy opt-out scheme.²⁹²

C. *Wealth Accumulation and the Retirement Objective*

The potential for wealth accumulation within the tax-qualified retirement plan context has been a longstanding bane of the tax-incentive nature of the voluntary pension leg of the triadic retirement income security stool. In discussing the evolution of the private pension system during the period spanning from the 1930s to the 1950s, one commentator's observations reveal:

The rise of class-based pension plans, both the collectively bargained and those serving management, were adjustments to the quickening American state. With the federal government providing basic retirement income [i.e., Social Security], private pensions became supplementary benefits The managerial plans emphasized asset accumulation and were often schemes for tax-sheltered savings as much as retirement income per se Labor plans stood at the opposite end. They were primarily welfare arrangements designed to provide adequate support to those in need.²⁹³

Retirement plan asset protection therefore is quite easily criticized as potentially serving mere wealth accumulation desires instead of retirement policy.²⁹⁴ But, this wealth accumulation potential must be more objectively evaluated because its presence within the carrot/stick incentive framework of the tax-qualification rules sheds light upon the particular role that asset protection might play in furthering federal retirement policy.²⁹⁵ Understanding that role demands an

291. The continuing applicability of 11 U.S.C. § 522(d)(10)(E) after passage of the Bankruptcy Amendments is discussed *supra* notes 271–75 and accompanying text. Regarding practical issues attendant a debtor-specific "reasonable needs" approach, see *infra* notes 328–33 and accompanying text.

292. The bankruptcy opt-out exemption scheme is the topic of *supra* Part IV.A.2.

293. SASS, *supra* note 62, at 143–44.

294. See, e.g., Dille, *supra* note 35, at 369 (criticizing protection of IRAs on the basis that such accounts allow accumulations "greatly in excess of any amounts reasonably necessary for retirement support").

295. The carrot-stick explanation of the tax-qualified plan regime is first discussed in *supra* note 121 and accompanying text.

inquiry that probes beyond the more simplistic wealth accumulation objection. In that regard, there are five specific observations to be noted.

First, at one time there were excise taxes that applied when distributions or plan accumulations grew too large.²⁹⁶ But, Congress recently repealed these excise taxes.²⁹⁷ This action could be characterized (like the repeal of wealth transfer taxes generally) as indicative of a lessening aversion to accumulated and potentially inheritable wealth or as a prevailing political desire to favor a more consumption-based tax regime.²⁹⁸ Notwithstanding these rationales, the excise taxes were clearly vulnerable because they acted as a burden upon the ratio of disincentive "sticks" in the tax-qualified plan regime. In other words, the repeal of these excise taxes represents tax-simplification that sweetens the overall retirement plan tax-incentive pot, but at some cost to equity given the enhanced retirement plan wealth accumulation potentials that resulted.²⁹⁹ The grant of properly focused asset protection could serve a similar incentive role.³⁰⁰

Second, rules requiring that certain minimum amounts must be withdrawn from tax-qualified arrangements beginning at the participant's attainment of a designated age mitigate, to some degree, the ongoing potential to accumulate wealth within these arrangements, although the possibility certainly remains.³⁰¹ But here again, recent legislative initiatives have simplified and liberalized certain distribution rules such that greater wealth accumulation within retirement plans is possible.³⁰² This liberalization could be cited as supporting either equity-based concerns about tax-driven asset protection,³⁰³ or as

296. See I.R.C. § 4980A, *repealed by* Pub. L. No. 105-34, § 1073, 111 Stat. 948 (1997) (imposing an excess retirement accumulation tax).

297. Pub. L. No. 105-34, § 1073, 111 Stat. 948 (1997).

298. See Martin A. Sullivan, *Administration Reignites Old Battle Over Tax Expenditures*, 91 TAX NOTES 701, 701 (2001) (discussing tax expenditures and Republican attempts to redirect the tax expenditure budget to more favorably impact their political preferences).

299. See Halperin, *supra* note 121, at 6-7 (discussing the tax incentive in relation to the compression of the progressive tax rate schedule, and noting: "At the same time as the stick (restrictions) has become heavier, the carrot (tax relief) has become less sweet." (footnote omitted)).

300. See *infra* Part V.C (discussing the ways in which asset protection can serve as an incentive).

301. See *supra* note 48 (discussing the requirements for certain minimum distributions from retirement plans).

302. See Holt, *supra* note 48, at 20 (discussing the proposed regulations for qualified plans and IRAs); Louis Mezzullo, *Proposed Legislation Will Simplify Distribution Rules*, TRUSTS & EST., Jan. 2001, at 41, 43-44 (explaining the benefits of recent legislative initiatives).

303. See *supra* Part III.C.2 (stating that the equity objection applies because the liberalized rules benefit higher wage earners, who are more readily able to contribute and then retain assets

supporting the notion that some sacrifice of equitable ideals are tolerable in the name of increasing the incentive/restriction ratio in the current tax-incentive regime. This duality highlights the difficult task of balancing wealth accumulation potentials, an adequate retirement benefit, and the problem of debtor access and control over account balances in a DC plan dominated environment.³⁰⁴

A third response is more clear in its implications—the tax-qualification regime imposes an objective limitation upon the tax-favored amounts that participants may contribute annually to a tax-qualified DC plan or IRA, or upon the annual amounts that may be distributed from a DB plan.³⁰⁵ Indeed, some commentators have viewed the wealth accumulation objection to asset protection under *Shumate* skeptically, calling that objection "dangerously myopic" and citing in support of their view the retirement plan contribution and distribution limitations imposed under the tax laws.³⁰⁶ In contrast to a debtor-specific and subjective case-by-case "reasonable needs" inquiry,³⁰⁷ for example, tying asset protection to tax-qualification and the attendant contribution/distribution limits would provide an objective boundary for the level of assets (in the case of a DC plan or IRA) or benefits (in the case of a DB plan) to be protected under the Federal Retirement Model.

This reasoning suggests a fourth response, which defers quite simply to the ease with which asset protection can be limited in the retirement plan context such that excessive contributions and eve-of-bankruptcy asset stashing can be thwarted.³⁰⁸ In fact, the Bankruptcy Amendments incorporate certain

in the plan); *infra* Part V.D (same).

304. See *infra* notes 308–12 and accompanying text (discussing this balancing in light of the prevalence of DC plans today). As to the distinction between DC plans and DB plans, see *supra* notes 93–102 and accompanying text.

305. See I.R.C. § 72(t) (2000) (imposing a 10% penalty on early withdrawals); *id.* § 401(a)(14) (setting forth the required beginning date for distributions to begin from tax-qualified plans); *id.* § 415 (imposing limits on contributions and benefits). Regarding the distinction between DC plans and DB plans, see *supra* notes 93–102 and accompanying text.

306. See Sabino & Clark, *supra* note 35, at 661–62 (discussing important concerns that the commentators objecting to *Shumate* fail to consider). More generally and with respect to the savings/retirement issue, scholars have noted the lower contribution limit for IRAs relative to employer-sponsored plans as consistent with the relationship among the three legs of the retirement income security stool. See, e.g., Graetz, *supra* note 58, at 901 (discussing the policy relationship between employer-sponsored plans and IRAs).

307. See *infra* notes 328–33 and accompanying text regarding practical problems with a case-by-case reasonable needs approach.

308. See Lawrence Ponoroff & F. Stephen Knippenberg, *Debtors Who Convert Their Assets on the Eve of Bankruptcy: Villains or Victims of the Fresh Start?*, 70 N.Y.U. L. REV. 235, 269–92 (1995) (reviewing and critiquing case law that confronts these debtor tactics).

safeguards along those lines, but for some reason restrict application of those safeguards to educational "IRAs."³⁰⁹ Expanding those safeguards to all protected retirement plans would help mitigate wealth-based objections to this protection.

Finally, modern trends in the prevailing types of retirement vehicles have inspired objection to the expansion of ERISA's asset protection features based upon the expedient of tax-qualification. Critics specifically cite the trend away from the employer-controlled DB plan environment that existed when the ERISA anti-alienation safeguards were originally conceived.³¹⁰ A more individual account-based, employee-dominated DC plan environment now exists.³¹¹ The problem pertains to the relatively greater access, control, and wealth accumulation potentials attendant to DC plans.³¹² Grafting asset protection onto this trend, however, inspires another more pragmatic conclusion. Specifically, to the extent investment returns within a DC plan exceed expectations such that unanticipated wealth is accumulated, the proffered asset protection is no less objectionable for DC plans than DB plans. This is because, from the employee-participant's viewpoint, the protection arguably provides a fitting offset to the broader trend away from safer DB plans (where investment and other risks lie with the employer) and towards the modern DC plan environment, which carries with it a shift in investment and other risks from employer to employee.³¹³ This linkage between increased employee investment risk and asset protection also is responsive to those who criticize tax-based asset protection as preserving assets rather than mere needs-

309. "IRA" is a misnomer, because the accounts have absolutely nothing to do with retirement, despite the "Individual Retirement Account" moniker. For a discussion of the limitations upon the protections afforded these tax-favored educational arrangements, see *supra* note 276. As to the presence of these asset protection limitations for education IRAs but not for standard or Roth IRAs, Congress perhaps deemed the fraudulent transfer provisions of the 1978 Code a sufficient direction from which other abuses might be contained, although this is far from clear. See, e.g., 11 U.S.C. § 548(a) (2000) (providing for avoidance of transfers made within one year of filing if made with actual or constructive intent to defraud creditors). For details of a failed proposal to limit the amount protected under the Bankruptcy Amendments, see Press Release, Office of Senator Chuck Grassley, Grassley, Sessions Seek Common Sense Reform to Protect Consumers, at <http://www.abiworld.org/resources/research/grasley.html> (May 2, 2000) (on file with the Washington and Lee Law Review).

310. For an asset protection objection that is articulated by reference to the trend away from DB plans, see Dilley, *supra* note 35, at 412–13.

311. For a discussion of this trend and the distinction between DB plans and DC plans, see *supra* notes 93–102 and accompanying text.

312. For an objection to asset protection articulated by reference to these trends and the resulting potentialities, see Dilley, *supra* note 35, at 412–13.

313. See *supra* notes 93–102 and accompanying text (discussing the nature of the DB and DC plans and the trend toward DC plans).

based income rights.³¹⁴ Responsiveness exists because the DC plan environment directly implicates the need to preserve *a base of assets* from which retirement benefits might ultimately be paid.³¹⁵ Wealth accumulation and preservation therefore are inherently necessary to the operative success of this prevailing retirement plan type. Once again, to the extent these asset protection arguments are rejected, the objection is really a more general attack on the overlying tax-qualified plan universe itself, and criticisms and reform suggestions should be thusly aimed. It is to these ideas that this Article now turns.

D. The Role of Equity and Prospects for Fundamental Reform

On the general point of retirement plan asset protection advancing policy objectives, "[f]ew would refute the sound reasons for protection of pension and retirement plans from the reach of creditors"³¹⁶ Yet, common to the criticisms of the current movement towards tax-qualification as relevant to asset protection is the overriding recognition that the grant of such protection can serve only to compound the inequities inherent in the nature of the retirement plan tax-incentive.³¹⁷ That incentive inures in large part to the benefit of higher-income taxpayers.³¹⁸ Hence, for the federal government to facilitate or even condone a further disconnect between lower wage earners and those of more substantial means would, in the eyes of many, add insult to injury by compounding the inequities wrought under the system as it currently stands. But the noted criticism misses the larger point. The focus should not be on inequity as an absolutely intolerable circumstance. The focus should be on the extent of equitable sacrifice that society can tolerate in pursuit of retirement policy goals and whether the proposed action sufficiently advances those goals.

1. An Impetus for Reform

The prospect of more closely linking asset protection to tax qualification provides a specific impetus for re-examining the current framework for

314. See *infra* notes 327–32 and accompanying text for a further exposition of this needs-based argument.

315. See *supra* notes 98–100 and accompanying text (explaining how DC plans work).

316. 1997 FINAL REPORT, *supra* note 184, at 139.

317. See the sources cited in *supra* notes 279–280 for those criticisms.

318. For a discussion of this equitable disparity, see *supra* Part III.D.

pursuing retirement income security goals. Should the equitable discrepancies—as specifically highlighted by the tying of asset protection more directly to the tax-incentive framework—be deemed unacceptable, the call should be for wholesale change in the current tri-part system of retirement income security. Many suggestions posed for restructuring the current tax-incentive retirement framework would render the system more inclusive across a broader range of employee income levels.³¹⁹ If asset protection were grafted upon a regime so revised, the resulting nexus between favored plans and the stated policy objectives, coupled with the posited reductions in systemic inequities, would make asset protection a desirable and patently inoffensive characteristic of a system so envisioned.³²⁰ The broader implication, then, is that a comprehensive solution to the retirement plan asset protection question may lie most fundamentally in revisiting the tax-incentive framework that currently serves as a primary means to pursuing retirement income security. Importantly, the current congressional momentum to more closely link asset protection to the tax-qualified retirement plan framework provides a new impetus for carrying out many of the reform suggestions aimed at improving retirement plan coverage, equity, and service to the overriding retirement income security goal.³²¹

2. Equity and Pragmatism

Short of such fundamental change, however, the extent of equitable sacrifice that is tolerated under the existing tax-qualified regime is telling. A walk down the pragmatic avenue of legislation in operation reveals that equity has long been an ambiguously effected objective of the federal government's

319. See, e.g., *supra* note 155 (discussing mandatory retirement provisions); see also Bankman, *supra* note 73, at 795–800 (discussing the regressivity of the payroll tax); Graetz, *supra* note 58, at 852–53 (discussing the tripartite system). See generally 21ST CENTURY, *supra* note 57, at 4–7 (discussing federal retirement policy's focus on providing adequate income post employment). The broader point here is that cogent ideas for reforming the existing system do exist and are both defensible and implementable.

320. See the discussion of the protections afforded a debtor's interest in Social Security entitlements in the text accompanying *supra* notes 81–82.

321. To the extent equity and redistributive objectives affect the analysis, the push should be in the direction of a more broadly-based and effective Social Security system or perhaps more universally mandated coverage of lower-wage employees, coextensive with asset protection for the resulting arrangements or interests. On the other hand, to the extent comfort exists with the notion of promoting not only minimally adequate but also living standard maintenance retirement savings, a logical course would be to focus upon more carefully crafting the contribution limits and withdrawal timing rules under the existing framework, and thereafter accepting the consequences across wage-earning scales.

approach to retirement income security.³²² Moreover, while commentators consistently keep the matter of equity in the forefront of perspectives on federal retirement policy,³²³ the pragmatic perspective again suggests that neither a positively redistributive scheme nor absolute parity across income levels has been a penultimate characteristic of the longstanding tri-part system of retirement income security. As noted earlier, for example, a broad view quickly reveals that the current retirement income security regime produces a two-class system.³²⁴ The distinction is between those who rely upon the base support of Social Security and those who are able to elevate their postemployment standard of living through supplemental resources like private pensions and personal savings.³²⁵ While certainly open to criticism, this reality is not simply the product of happenstance or poorly crafted legislation. Rather, it is to some degree a recognized incident of the "lifestyle maintenance" facet of the federal government's three-pronged approach to accomplishing its retirement policy objectives.³²⁶ The direct implication is that within the existing retirement policy context, some disparate benefit is warranted so long as a lifestyle maintenance component of the policy objective is adhered to and actively pursued.

3. *A Problem at the Equitable Border*

Of course, one should not overlook the possibility of defining the proper bounds of asset protection as lying at the border between basic needs and lifestyle

322. The focus here is on vertical equity, which in tax parlance focuses on the disparate treatment of persons across income levels. In contrast, the idea of horizontal equity examines the treatment of similarly situated persons. See Halperin, *supra* note 121, at 48–49 (discussing vertical and horizontal equity considerations in context of tax-qualified retirement plans); Stein, *supra* note 130, at 226–27 (same).

323. See, e.g., *supra* notes 145–59 (discussing the trade-off of equity and tax expenditure).

324. See *supra* note 148 and accompanying text (discussing a two-class system of retirement).

325. See Altman, *supra* note 58, at 501–02 (discussing the three-legged stool analogy to the U.S. system of retirement income security). SASS, *supra* note 62, states:

Approaching private pensions from two different directions, government policy in the 1930s thus defined an intermediate *public* role for employer-sponsored plans: they would provide *socially* needed supplementary retirement income to an upper-middling segment of the population. Social Security would provide the basic leg of the elderly's new three-legged stool; the combination of tax benefits, IRS regulations, and employer interests would maintain private pensions as the intermediate support for middle-class Americans.

Id. at 111.

326. See *supra* notes 62–63, 75–77, 84–87 and accompanying text (discussing the lifestyle maintenance aspect of the retirement income security objective).

maintenance, as some have argued.³²⁷ This more limited grant of asset protection clearly is the better option if absolute equity across employee income levels is the guiding principle. Bare appeals to this equitable ideal, however, are too superficially respectful of other considerations affecting national retirement policy, such as the desire for some measure of lifestyle maintenance. Moreover, certain practical problems arise when the legislature attempts to apply a more limited grant of asset protection within the retirement plan context.

For example, some commentators see within the § 522(d)(10)(E) federal exemption framework a basis for reconciling ERISA's retirement income security goals with the fresh start/marshalling of assets principles of bankruptcy law.³²⁸ Reconciliation occurs through the harmonization of competing principles that arguably results from the case-specific and protection-limiting "reasonable needs" analysis under current § 522(d)(10)(E). Of course, this approach assumes in the first instance that there is some outstanding need to reconcile the retirement income security policies of ERISA with the 1978 Code's marshalling of assets/fresh start concerns, in seeming contravention of the Supreme Court's conclusion that Congress already has made a clear policy decision favoring retirement income security.³²⁹

From a more practical standpoint, an extensive congressionally commissioned 1997 report expressly condemns needs-based and similar fact-specific federal exemption standards.³³⁰ That report criticizes those standards as being too dependent "upon subjective judicial determinations of what would be 'reasonably necessary' for [a given] debtor."³³¹ The report further notes that "[t]his fact-based test can lead to excessive litigation or intrusive and time-consuming inquiries," and other commentators agree.³³² Indeed, the evaluation

327. See, e.g., Dilley, *supra* note 35, at 410–13 (discussing problems with the fresh start principle).

328. See Michelle M. Arnopol, *Including Retirement Benefits in a Debtor's Bankruptcy Estate: A Proposal for Harmonizing ERISA and the Bankruptcy Code*, 56 MO. L. REV. 491, 559 (1991) (stating a proposed solution that includes repeal of 1978 Code § 541(c)(2) coupled with exemption approach of 11 U.S.C. § 522(d)(10)(E) but with specific guidelines to assist courts in "reasonably necessary" determination); Dilley, *supra* note 35, at 410–13 (attempting to reconcile ERISA and 1978 Code policies through the 11 U.S.C. § 522(d)(10)(E) limitation); Wohl, *supra* note 35, at 31–36 (proposing reconciliation of ERISA and 1978 Code policies). Regarding 1978 Code § 522(d)(10)(E), see *supra* notes 235–61.

329. See *supra* notes 221–22 and accompanying text (discussing the Supreme Court's decisions in *Shumate* and *Guidry*).

330. See 1997 FINAL REPORT, *supra* note 184, at 139–40 (stating that fact-based tests "can lead to excessive litigation or intrusive and time-consuming inquiries").

331. *Id.*

332. *Id.* Emanuel, *supra* note 20 states:

called for under a broadly applicable reasonable needs approach reflects a paternalistic judgment that is inconsistent with some of the philosophies underlying the current three-legged stool of retirement income security:

The combination of private entitlements to future income in old age—such as individual annuities and insurance as well as employer-provided pensions—with the public entitlement of Social Security resulted in a system of individual rights to accumulate as much or as little retirement income as fortune or choice would allow. The earned entitlement, under the American system, was the opportunity to accumulate. The guarantees were not to any level of income but rather to payments from specified sources, which might amount to adequate, inadequate, or even excessive income, but which were designed to avoid imposition of adequacy measures from external authority.³³³

The point here is not to argue that equitable concerns are unimportant. Rather, the point is that, in considering equitable disparities resulting from asset protection outcomes under the Federal Retirement Model, a degree of both reason and reasonableness exists in the guise of the retirement income security objective, the due regard for its base income *and* lifestyle maintenance parameters, and the mechanisms underlying the tri-part approach to its achievement. Shortcomings with that logic highlight problems with the existing retirement plan structure more so than with asset protection per se. A more carefully tailored approach to ensuring that the retirement plan mechanisms employed actually do serve the underlying retirement policy objectives would go far in addressing those concerns.³³⁴ But ultimately, viewing the question as one pertaining solely to the three-legged stool of

[W]hile a needs test would destroy much of the utility of the spendthrift provision to the rich and answer the criticism that one should not enjoy a luxurious income without meeting one's obligations, a needs test would impose intolerable transaction costs by requiring the claimant to establish that the beneficiary was not needy enough to qualify for [protection].

Id. at 191; Lawrence Ponoroff, *Exemption Limitations: A Tale of Two Solutions*, 71 AM. BANKR. L.J. 221, 224–25 (1997) (criticizing a case-by-case approach to the proper bounds of exemption planning as leading to inconsistency, ambiguity, and frustration among both courts and debtors); Wohl, *supra* note 35, at 34 ("The difficulty with this analysis [tied to 11 U.S.C. § 522(d)(10)(E) concepts] is that there is no analytical basis . . . on which the courts have drawn the line between those too young to have such assets protected and those too old to permit assets to be available to creditors."); *id.* at 35 ("How much the 'reasonable retirement amount' should be is difficult to say and is . . . beyond the scope of this Article.").

333. Dilley, *supra* note 66, at 1108; *see also supra* note 328 (discussing a reasonable needs approach as a means of reconciling ERISA's retirement income security goals with principles of bankruptcy law).

334. For a discussion of asset protection as an impetus for reforming the current retirement plan structure, see the text accompanying *supra* notes 319–21.

retirement income security is too narrow a focus. Instead, the other triadic relationship revealed in this Article must be considered. That relationship is, of course, between the Traditional, Self-Settled, and Federal Retirement Models of asset protection.

E. There and Back Again: Resolution Across the Models

Exploration here of the evolution of asset protection within the Federal Retirement Model revealed an initial tendency to set retirement plan asset protection parameters by reference to traditional and self-settled spendthrift trust considerations.³³⁵ The 1992 *Patterson v. Shumate* decision caused a firm break in that analysis, leaving a Federal Retirement Model that is disjointed in its approach to asset protection.³³⁶ As movements in the legislative arena now promise, or threaten, to heal this rift through the clear linkage of asset protection to retirement plan tax-qualification criteria,³³⁷ a comprehensive view of the issue demands that interactions across the three models of asset protection not be forgotten along the way.³³⁸ In direct contrast to the flow of traditional influences originally affecting asset protection developments within the Federal Retirement Model, the influence of federal retirement policies should now dominate future movements in defining the availability of asset protection in more traditional settings. Specifically, retirement policy concerns demand a re-examination of asset protection as it affects the Traditional and Self-Settled Models. That re-examination reveals that retirement policy objectives provide a purposive benchmark by reference to which asset protection should now be granted.

1. A Risk of Hypocrisy

An ideally purposive Federal Retirement Model would only protect interests that are directed towards service to the goal of retirement income security. The potential interaction between this ideally purposive Federal Retirement Model and the merely protective Traditional and Self-Settled Models raises an important question: Why do we deem considerations of

335. See *supra* Part IV.B.1 (discussing the initial stage of post-ERISA protection).

336. For a discussion of *Patterson v. Shumate*, 504 U.S. 753 (1992), see *supra* Part IV.B.2.

337. See *supra* Part IV.C (discussing recent congressional action concerning retirement plan asset protection).

338. For an explanation of the Traditional, Self-Settled, and Federal Retirement Models, see the text accompanying *supra* notes 40–42.

purpose and equity so relevant to defining and evaluating retirement plan asset protection, yet we seem to have cast those same considerations aside for little apparent reason (apart from federalism concerns) in the related trust contexts? The careful effort to craft a regime of creditor-protected retirement interests through attention to an acceptable association between those interests and meritorious federal retirement policy goals ought to foreclose a unilateral grant of unbounded asset protection—fostered through federal mechanisms like § 541(c)(2)—absent the advancement of some similarly meritorious purpose that goes beyond blind deference to historical federalism principles and the property rights rationale thereby supported.³³⁹ As long as the contrast endures through a lack of federal attention to those matters, asset protection as an end unto itself will continue to dominate developments across the models. Those developments include, for example, the recent acceptance of the domestic self-settled asset protection trust.³⁴⁰ Extrapolating those progressions to an area of more direct federal concern reveals that, without more comprehensive attention, further efforts to define the proper boundaries of asset protection within the context of federal retirement policy may be co-opted by the practical reality that "[r]etirement plans represent a major planning opportunity for asset protection . . . [pursuant to which] substantial sums can be shielded"³⁴¹ Perpetuating an environment wherein participants view retirement plans as merely one of several devices for use in thwarting creditors also circuitously thrusts the analysis back under the weight of criticism grounded in the characterization of retirement plans as mere wealth accumulation devices. The proper response lies in more careful consideration of that characterization, coupled with an approach that distinguishes retirement plans from other asset protection devices based on service to larger federal goals.³⁴²

For example, many have criticized the now viable Self-Settled Model as fundamentally undermining federal bankruptcy policy by permitting

339. See *supra* Part II (presenting historical arguments supporting spendthrift trust asset protection); see also *supra* Part IV.A (discussing 1978 Code § 541(c)(2)).

340. See the text accompanying *supra* notes 49–55 regarding the rise of domestic self-settled asset protection trusts in contravention of over a century of accepted spendthrift trust doctrine.

341. SPERO, *supra* note 212, at 10–41.

342. For a critical evaluation of the characterization of retirement plans as mere wealth accumulation devices and the relationship of that characterization to asset protection, see *supra* Part V.C. The author makes that evaluation by reference to retirement policy goals and asset protection's potential service to those goals. The irony noted here is that, without more thoughtful consideration of furthering that service, tying asset protection to tax-qualified retirement plan status—without due regard for the broader asset protection environment—does little to distinguish the retirement plan genre from the asset protection currently available under the Traditional and Self-Settled Models.

prospective debtors to essentially "endow" themselves without regard to any fresh-start or other socially conscious concerns.³⁴³ Some have therefore concluded that congressional action is necessary to thwart this end-run around the debtor-creditor framework of federal bankruptcy laws.³⁴⁴ Were Congress to move towards that objective without correspondingly tightening the controls on withdrawal and non-retirement use of tax-qualified retirement plan assets—or without at least capping the protection afforded some of the more troublesome arrangements like IRAs (as proposed under the Bankruptcy Amendments)—a tangible degree of hypocrisy would stem from the leakage inherent in the existing lax retirement plan withdrawal rules.³⁴⁵ The inconsistency lies in the prospect of Congress (or even the federal courts) acting to eliminate unguided settlor asset protection in the self-settled trust context, while allowing such a protective framework to remain essentially intact for liberally accessible retirement plans. The association between retirement plans and self-settled trusts arises by virtue of employee (settlor) ease of access to retirement account funds that the employee contributed.³⁴⁶ Considering that those funds also enjoy the added benefits of tax-qualification with respect to the accumulation process,

343. A debtor achieves this by stashing assets in a trust of which the debtor is both settlor and beneficiary, and which will allegedly thereafter be immune from creditor claims by virtue of jurisdictional trust legislation and bankruptcy estate exclusion under § 541(c)(2). *Supra* notes 49–55.

344. See, e.g., Henry J. Lischer, *Domestic Asset Protection Trusts: Pallbearers to Liability?*, 35 REAL PROP. PROB. & TR. J. 479, 534–36 (2000) (arguing that asset protection trusts are objectionable because they permit debtors to avoid lawful debts); Sterk, *supra* note 20, at 1114–17 (contemplating whether legislation should play a role in regulating asset protection trusts). For a discussion of self-settled trusts, see *supra* notes 49–55 and accompanying text. It should be noted that these self-settled trusts may have certain vulnerabilities to creditor claims under federal bankruptcy laws. See *supra* note 52 (discussing conflicts of law issues); see, e.g., Boxx, *supra* note 20, at 1208–40 (discussing arguments that may undermine effectiveness of self-settled trusts); Sterk, *supra* note 20, at 1074–1104 (same). As to calls for congressional action and even criminal sanctions in the arena of asset protection trusts, see Randall J. Gingiss, *Putting a Stop to "Asset Protection" Trusts*, 51 BAYLOR L. REV. 987, 1005–08 (1999) (stating that congressional action is appropriate when contempt of court actions fail as deterrents); Sterk, *supra* note 20, at 1114–17 (concluding that criminal sanctions may be the only viable deterrent).

345. For the cap on asset protection for IRAs as proposed under the Bankruptcy Amendments, see *supra* note 276 and accompanying text. For a discussion of the idea of retirement plan "leakage," see *supra* notes 286–87 and accompanying text. For an argument *against* capping even the amount sheltered in IRAs, see the remarks of Senator Kennedy (D-Mass.) in 147 Cong. Rec. S2151–S2152 (daily ed. Mar. 12, 2001) ("The provision in the bankruptcy bill that would cap the amount of retirement savings held in individual retirement accounts that can be exempted from a debtor's bankruptcy estate is a step backwards The IRA was developed as a retirement account basically for working families.").

346. Regarding employees as retirement plan "settlers," see *supra* notes 55 and 212–13.

the irony of addressing only non-"retirement" self-settled arrangements is evident.³⁴⁷

At a minimum, a course more consistent with a purposive Federal Retirement Model would be to impose a dollar cap upon the protection afforded traditional and self-settled trust arrangements under federal bankruptcy principles—just as in the case of IRA treatment under the Bankruptcy Amendments.³⁴⁸ To the extent federalism concerns continue to push for some recognition of state law trust protections, the government can still respect donors' freedom to craft protective trust interests by continuing to recognize those interests that terminate upon creditor action.³⁴⁹ This would confine to the retirement context the idea of *ongoing* beneficiary enjoyment garnered through spendthrift protection.³⁵⁰ In short, the growing attention paid to the proper bounds of asset protection in the retirement plan context suggests that freedom to accumulate and to dispose fall short of compelling justifications for bestowing federally sanctioned but unlimited asset protection upon traditional or self-settled spendthrift trust vehicles. The absence of such limitations is by no means a necessary characteristic of the existing framework.³⁵¹

347. For a discussion of the idea of retirement plans as mere wealth accumulation devices, see *supra* Part V.C. Retirement plan tax incentives are the topic of *supra* Part III.C.

348. See *supra* note 276 and accompanying text (discussing the cap imposed on standard and Roth IRAs).

349. The reference is to protection afforded a trust beneficiary through operation of what is commonly referred to as a forfeiture restraint, which is less objectionable than asset protection obtained through operation of spendthrift restraints. Most simply, a forfeiture restraint provides that the beneficiary's interest will *terminate* upon the beneficiary's bankruptcy or any attempt by the beneficiary or her creditors to alienate the beneficiary's equitable trust interest. Through default gifts over to other beneficiaries named in the trust instrument, the settlor directs the successor to the beneficiary's interest. The law has long permitted trusts including such *indirect* restraints, notwithstanding the continued rejection in England of the more direct spendthrift restraint. See, e.g., 1 RESTATEMENT (SECOND) OF TRUSTS § 150 (1959) (describing and recognizing that type of forfeiture provision as valid); IIA SCOTT & FRATCHER, *supra* note 18, § 150 (1987) (discussing forfeiture provisions). Spendthrift restraints are more likely than forfeiture restraints to achieve the settlor's dual goals of providing for the beneficiary while thwarting creditors because the beneficiary protected by virtue of a spendthrift restraint need not forfeit her interest when faced with a creditor claim. Instead, the beneficiaries retain the prospect of further enjoyment of their trust interests notwithstanding the thwarted creditors' efforts to reach those interests or the trust property supporting them.

350. Regarding objections to the protected but retained enjoyment of a spendthrifted trust interest, see *supra* note 23 and accompanying text.

351. See GRISWOLD, *supra* note 20, § 552 ("[T]he major premise [underlying this spendthrift trust justification]—that the owner of property may dispose of it as he desires—is patently fallacious."). With regard to the freedom of disposition rationale for spendthrift trusts, see the text accompanying *supra* note 27.

2. Protecting the Incentive

The availability of asset protection to motivate people to participate in federally sanctioned retirement plans also deserves more direct consideration. This incentive potential informs the question of why Congress should more carefully consider the undercurrent of influence among the three asset protection models and why that consideration should ripen into a less passive, more comprehensive approach to asset protection. To the extent the incentive potential of asset protection is not self-evident, it is easily extrapolated by analogy to the premise underlying the retirement plan *tax* incentive.³⁵² The New York Bar Association's Special Committee on Pension Simplification recently spun that premise quite practically:

It would be naive to minimize the lure of a tax shelter as an important contributor to the success of the private pension system, which, in the small plan universe at least, is often due at least as much to the owner's search for personal financial security as to his concern for the retirement security of his employees.³⁵³

Indeed, other commentators have more directly stated that the special status derived from the ERISA anti-alienation and preemption provisions "enhances the value of compensation paid in the form of retirement benefits and thus promotes retirement plan participation and sponsorship."³⁵⁴ This asset protection incentive also comes at no detriment to the federal budget, in contrast to the tax expenditure cost associated with the retirement plan tax-based incentive.³⁵⁵ While some might argue that the cost of retirement plan asset protection would be more subtle in terms of impact upon the market for consumer credit with further implications on the market economy, those assertions are unfounded, or at best, tenuous.³⁵⁶

352. See *supra* Part III.C regarding the tax incentives for retirement plan participation.

353. Alvin D. Lurie, *ERISA: A Process Still Awry, A Need to Simplify*, 83 TAX NOTES 1053, 1055 (1999).

354. van Zante, *supra* note 119, at 144; see *Boggs v. Boggs*, 520 U.S. 833, 841 (1997) (describing ERISA's express preemption clause).

355. See the discussion of tax expenditures *supra* notes 150–58 and accompanying text.

356. See *In re Baker*, 114 F.3d 636, 640 (7th Cir. 1997) ("When it extended the credit that it [now] seeks to collect from [the debtor's] (remaining) interest in [a retirement plan that was a spendthrift trust], the [creditor] knew or should have recognized that this wealth could not be reached in a bankruptcy action."); JCS-16-91, *supra* note 35, at 11 ("Plan benefits generally are not taken into account in credit extension decisions because they are not available as security."); Adam J. Hirsch, *Inheritance and Bankruptcy: The Meaning of the "Fresh Start"*, 45 HASTINGS L.J. 175, 194 (1994) ("[L]awmakers have found compelling policy reasons for denying creditors the opportunity to rely on certain interests of the debtor in the event she becomes insolvent."); Ponoroff, *supra* note 332, at 233 ("Creditors make credit decisions with full knowledge of the

Viewing the asset protection component of the retirement plan legal structure as a potential incentive leads to another important conclusion that can be derived by analogy to the operation of the retirement plan tax incentive. That analogy directly supports the notion that Congress should incorporate a more comprehensive view of asset protection into federal retirement policy. Specifically, in the context of the retirement plan tax-incentive, a corresponding *denial* of similar tax benefits *outside* the tax-favored plan universe is critical to the effectiveness of that tax incentive.³⁵⁷ In other words, the reasoning goes, there would be a general disinclination to subject oneself to the restrictions and operative rules (i.e., the "sticks") that accompany retirement plan tax-qualification if equivalent tax-deferral and tax-free earnings potential (i.e., the "carrots") were available outside the strictures of the tax-qualified plan universe.³⁵⁸ Similar to the tax-incentive "carrot," dangled before taxpayers as an offset to the restrictive rules that encourage the funding and maintenance of particular types of retirement plans, uniquely available asset protection might serve a similar incentive role. The availability of multiple avenues to asset protection via the Traditional and Self-Settled Models, in turn, would then blunt the ability of Congress to employ the concept of asset protection in furtherance of federal retirement policy objectives. As one noted commentator specifically observed regarding the tax incentive: "the existence of . . . equivalent [advantages not directed towards retirement] . . . through less

applicable exemption scheme, and, absent a valid security interest, with knowledge of the debtor's right to freely alienate his or her property . . ."). Ponoroff further observes that the failure to respect the debtor's planning opportunity in this regard would result in an unwarranted windfall to creditors. *Id.* at 233. In the context of creditor access to property held in a traditional spendthrift trust, Professor Costigan observed that it would be "curious to have the creditor of a cestui [i.e., beneficiary] so exalted in position and honor . . . that he must be given even all the property," and that "the creditor is seeking to reap where he has not sown . . . It is moral theft . . ." Costigan, *supra* note 23, at 476-77.

357. Graetz states this point directly:

It is clear that the private pension system depends upon encouragement by high-earning employees for the creation and maintenance of employer-sponsored retirement plans that redistribute to low- and moderate-income workers at least a portion of the tax savings This goal is made more difficult, however, whenever there exist other opportunities for high wage earners to achieve equivalent tax savings without the kind of restrictions applicable to employer-provided pension plans.

Graetz, *supra* note 58, at 87; see also Halperin, *supra* note 121, at 38 ("If . . . qualified plans are threatened by a potential shift to nonqualified arrangements, greater penalties on nonqualified deferred compensation should be considered.").

358. For the initial discussion of the carrot-stick explanation of the tax-qualified plan regime, see *supra* note 119 and accompanying text. See *supra* Part III.C for a discussion of tax deferral and tax-free earnings.

restrictive alternatives . . . may inhibit the ability of Congress to fashion those restrictions on tax-preferred savings that would best serve national retirement security policy."³⁵⁹

Similarly, to the extent Congress curtails less restrictive planning opportunities such as those offered through the Traditional and Self-Settled Models, the availability of retirement plan asset protection becomes both more noticeable and more enticing to anyone able to grasp the benefits of setting aside funds today in a tax-favored, creditor-sheltered vehicle in order to better finance a retirement promise that is widely recognized as a mantra of modern American life.³⁶⁰ Simply stated, federal retirement policy objectives can be advanced through a more comprehensive understanding and treatment of asset protection. Equitable concerns attributable to differences across wage scales and the relative opportunity to capitalize upon the retirement plan asset protection enticement affect this assertion, but neither defeat it nor necessarily imply that retirement plan asset protection extending beyond mere base-level income maintenance is ill-conceived.³⁶¹ Rather, those concerns suggest broader social policy choices that Congress should expressly consider in the context of the objectives and mechanisms underlying retirement income security, with asset protection informing important aspects of that debate.

VI. Conclusion

Traditional and self-settled spendthrift trust concerns, coupled with seemingly disjointed congressional actions, have shaped a divided landscape of retirement plan asset protection. Certain retirement plans currently receive a grant of blanket asset protection without further inquiry, while others continue to receive careful scrutiny based upon criteria derived from analysis typically ascribed to the Traditional and Self-Settled Models or to exemption laws more generally. The movement to gauge retirement plan asset protection by reference to tax-qualified status raises questions about how well that status, or asset protection linked thereto, truly serves the broader goal of retirement income security. Focusing upon the broader asset protection landscape from a view tinted by federal retirement policy concerns ultimately draws attention to the need for a less passive, more comprehensive congressional treatment of

359. Graetz, *supra* note 58, at 902.

360. See, e.g., Dille, *supra* note 35, at 368 (noting "the cultural significance of the retirement phenomenon, which has taken on the status of a right, rather than a choice").

361. See, in this regard, the discussion of the anti-poverty and lifestyle maintenance components of the retirement income security objective set forth in *supra* notes 62–64.

those species of asset protection that are unbounded by any principled purpose. Retirement policy objectives provide that purpose. Congress should view those objectives as a benchmark for defining asset protection boundaries, thus placing the concept of asset protection in direct service to federal retirement policy goals. That benchmark, in turn, should then guide: (1) the grant of federally-sanctioned asset protection within the retirement plan setting; and (2) the denial of such protection in the context of more traditional trust devices that do not further any discernable federal purpose.